United States Court of Appeals

for the Second Circuit

APPENDIX

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United States Court of Appeals
FOR THE SECOND CIRCUIT

Docket No. 75-1004

UNITED STATES OF AMERICA,
Appellee,

v.

ANTHONY M. NATELLI, and
JOSEPH SCANSAROLI,
Defendants-Appellants.

JOINT APPENDIX
VOLUME IV
Trial Testimony, Pages 1471 to 2459

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UNITED STATES COURT OF APPEALS
FILED
APR 3 1975
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

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(Witness excused.)

xx H A R V E Y J. C L A W S O N, called as a witness by the defendant Scansaroli, having been first duly sworn by the Clerk of the Court, testified as follows:

MR. STILLMAN: Call Mr. Harvey Clawson.

xx DIRECT EXAMINATION

BY MR. STILLMAN:

Q Mr. Clawson, I'm going to ask you to speak right out so these ladies and gentlemen can hear what you have come to tell us.

Where do you live, sir?

A I live in Ebensburg, Pennsylvania, Cambra County.

Q How long have you lived in that part of the country, sir?

A All my life, 51 years.

Q Do you know Joseph Scansaroli?

A I do.

Q By the way, what is your occupation, sir?

A I'm a steel worker, Bethlehem Steel Company; part time police chief in the Township where I live.

Q How long have you been with Bethlehem Steel?

A 26 years.

Q How long ago was it that you met Joseph Scansaroli?

A I met Joe back in the early fifties, first part of

1950, '51.

Q I gather you have continued to know him over the years. Of course, there was a time that he left that area and then, of course, came back, is that right?

A Absolutely, yes.

Q Do you live nearby to him?

A I live practically, say a neighbor, a couple of houses away.

Q You don't measure in blocks in Ebensburg, do you?

A No, not out there where we live, you don't. It's a rural area.

Q Do you know other people in the community who know Joseph Scansaroli?

A I know pretty near everybody in that area. Most everybody knows Joe. Joe was my ~~sixteen~~ assistant scout master back in the early 50's, had about 35 boys. Most of them boys are there, too, in that area. They all know Joe.

Q Do you know what Joseph Scansaroli's reputation is for honesty, integrity, truth and veracity?

A You couldn't say anything against Joe in that part of the country whatsoever. Joe is honest.

MR. STILLMAN: Thank you, sir.

xx CROSS EXAMINATION

BY MR. VELIE:

Q Mr. Clawson, did you come up last night?

A I flew up last night. We get in about 10.

Q Thank you for coming.

THE COURT: Thank you, sir. You may be excused.

(Witness excused.)

MR. STILLMAN: Albert Zanzuccki.

xx A L B E R T A. Z A N Z U C C K I, called as a witness on behalf of the defendant Scansaroli, having been first duly sworn by the Clerk of the Court, testified as follows:

xx DIRECT EXAMINATION

BY MR. STILLMAN:

Q Dr. Zanzuccki, where do you live, sir?

A Ebensburg, Pennsylvania.

Q What is your occupation?

A I am Chairman of the Department of Business Administration at St. Francis College, Loretta, Pennsylvania.

Q Would you try to keep your voice up a little bit, please, sir.

What is your educational background?

A I received my undergraduate degree at Indiana State University at Indiana, Pennsylvania, my Masters at the University of Pittsburgh and my Doctorate at Penn State University State College, Pennsylvania.

Q That Doctorate is in education, sir?

A It is in education and finance.

Q How long have you been teaching at St. Francis College?

A This is my 29th year.

Q In addition to teaching at the school, do you maintain an accounting practice in that area?

A Yes, I do. I have an accounting practice with another partner, Mr. Kuzemchak.

Q Zanzuccki and Kuzemchak?

A Yes, sir.

Q Do you know Joseph Scansaroli, sir?

A Yes, I do.

Q How long have you known him?

A All my life, and I might say that not only knowing him, I know his paternal grandmother and paternal grandfather and material grand mother and material grandfather.

Q How have your paths crossed, that is, how apart from the family relationship, how else have you and Joseph Scansaroli come to know each other?

A Mr. Scansaroli was also a student of min e when he attended St. Francis College. I have had him in class and I have had -- I got to know him very well through class participation and also as Chairman of the Department of Business Administration.

Q Did you play any role in his determination to attend St. Francis College?

A Yes, I did.

Q How did that come about?

A After the services I had occasion to talk to his Dad and his Dad told me that he was -- his son was interested in going to college. So I convinced him that that was the proper thing to do and the father then talked to his son and he enrolled at St. Francis College.

Q What was his father's occupation, sir?

A His father was a miner.

Q Apart from Joseph being a student of yours, have you and he come to have any professional relationship?

A Yes. I have a limited practice in accounting because my duties at the college take quite a bit of my time. So when a person is looking for some accounting work I would refer them to Mr. Scansaroli.

Q Have you had occasion to talk to those people and to others with respect to Joseph's reputation for honesty and integrity, truth and veracity?

A Yes, I have. As I -- being an educator you always want to follow up and I would contact these various clients and ask them about Joe and they spoke very highly about his honesty and integrity.

Q If you had to choose a word to summarize his reputation for those qualities, what word would you choose, sir?

A I think I would choose excellent.

MR. STILLMAN: Thank you very much, Doctor.

Your witness.

CROSS EXAMINATION

BY MR. VELIE:

Q Dr. Zanzuccki, thank you for coming. I take it you came up last night as well, is that the idea?

A Yes, I did.

Q In that case you haven't heard any of the accounting proofs in this case, have you?

A No.

Q The witnesses or examined the work papers?

A No, I haven't.

MR. VELIE: Thank you.

THE COURT: Thank you, sir. You may be excused.

THE WITNESS: Thank you.

(Witness excused.)

MR. STILLMAN: Call Joseph Scansaroli.

J O S E P H S C A N S A R O L I, called as a witness on his own behalf, having been first duly sworn by the Clerk of the Court, testified as follows:

DIRECT EXAMINATION

BY MR. STILLMAN:

Q Mr. Scansaroli, Joe, you know I have a somewhat

loud voice. I would like you to talk right out to me so that the ladies and gentlemen can hear everything that you have to say. Would you try to do that, please?

A Yes, sir.

Q How old are you?

A 38.

Q Where are you now living?

A Near Johnstown, Pennsylvania.

Q What is the name of that community that you live in?

A It is Ebensburg, a small community.

Q Were you born and raised in that area of the country, sir?

A Yes, I was.

Q A town called Nanty-Glo?

A That's right.

Q After completing your high school education there did you go on to serve in the United States Army?

A Yes, I did.

Q How long were you in the Army?

A For three years, from 1955 to 1958.

Q You were honorably discharged?

A Yes, sir.

Q Following your discharge what did you do?

A About a month after I was discharged I began at St. Francis College.

Q When were you graduated from St. Francis?

A February 1962.

Q What degree were you awarded?

A A B,S. Degree in accounting.

Q At that time did you leave the Ebensburg-Johnstown area?

A Yes. About a week or two weeks after I graduated I went to Washington, D.C.

Q Was there any reason you chose Washington, D.C. as a place to settle?

A Yes, my brother had gone there before me and I felt if I was going to work some place that was as good as any, since he was there, and I thought maybe Icould keep an eye on him.

So I went to Washington, D. C.

Q Did you go to work when you got to Washington?

A Yes, I did.

Q Who did you first work for in Washington?

A I started with a small accounting firm.

Q Do you recall the name of that firm?

A I don't recall the name, no.

Q After a short period of time with that firm, did

you become employed by the Washington office of Peat, Marwick, Mitchell?

A Yes, I did.

Q Approximately when do you place that in time?

A About July 1962.

Q Joe, I am going to have to ask you to keep your voice up. I am straining a little bit. If you don't mind, please.

A Okay.

Q What was your first position with Peat, Marwick?

A I was an assistant accountant or junior accountant.

Q What was the nature of the duties that you performed as a junior accountant?

A A junior accountant usually does most of the detail work on an audit. That is, he does the test work, the footing, things of that nature.

Q Did there come a time when your status changed from junior accountant to something else?

A Yes. I believe about 1965 I was promoted to senior accountant.

Q Did the nature of your duties change with your promotion to senior accountant?

A Yes, they did.

Q If you can briefly describe for the ladies and gentlemen of the jury, what were you then doing?

A Well, I did less of the detail work. I was in a position where I would maybe supervise some of the junior accountants that were coming in.

Q Did anything else happen to you in 1965 insofar as your professional career was concerned?

A I believe that's the time that I passed the CPA examination.

Q You became a certified public accountant in Washington, D. C.?

A That's right.

Q Directing your attention to 1967, did your position change at that time at Peat, Marwick?

A Yes. I was promoted to supervisor.

Q Once again, did your duties change from those that had previously been during the time that you were a senior?

A Yes, they did.

Q Would you please tell us in outline form what this next change was.

A A supervisor generally is responsible for a number of clients. He may be responsible for from anywhere from 10 to 15 clients. He is responsible for scheduling the audits,

scheduling the people to work on the audits, reviewing work papers, having conferences with the clients on matters that they may raise, things of that nature.

Q Can you tell us whether as an accountant working for Peat, Marwick, Mitchell you had any financial interest whatsoever in any of the accounts that you were servicing?

A No, sir.

Q As a matter of fact, that is prohibited, is it not, so that the auditors may maintain their independence from the clients?

MR. VELIE: Your Honor, at this point we are past preliminaries. I am going to ask Mr. Stillman not to lead.

THE COURT: All right.

MR. STILLMAN: Sustained, your Honor?

THE COURT: No, we will let this one stand.

MR. STILLMAN: Thank you.

THE COURT: But I don't think Mr. Scansaroli needs be led.

MR. STILLMAN: I have no intention of doing that, Judge Tyler.

Q Will you tell us why an auditor with a public auditing firm cannot own any financial interest in the clients that he is working on?

A Because the CPAs are independent auditors. If you have a financial interest in a company you cannot be considered independent.

Q I would like to now move ahead to the period around the summer of 1968. Can you tell us whether or not during that period of time you were busy or were things quiet? How would you characterize thenature of your work in broad form at that time?

A I think during the period from 1967 to about the middle of 1969 we were extremely busy, not only in our office, but in all the other offices throughout the country.

Q I would just like to direct our attention to your office and to you in particular. About how many client were you servicing at that period of time?

A At that point in time it could have been anywhere from 8 to 12 to 15 clients.

Q Do you recall the names of any of them?

A D.C.Transit, Folger, Nolan, Fleming, Avemco Corporation, Steadman Securities. Those are ones I can recall.

Q How many hours a day were you working in that

period of time, around the summer of 1968 and forward?

A I think on the average we were working 10, 11 hours a day, five days a week, plus a good many Satursdays.,

Q Do you get paid overtime?

A No, sir, not as a supervisor.

Q And you were a supervisor at that time?

A Yes, sir.

Q When for the first time in your life did you hear of National Student Marketing Corporation?

A It was about the last week in August of 1968.

Q Will you tell us how it came to be that you heard of this particular public corporation?

A I was working at a client's office outside the office when Mr. Natelli called me and wanted to know if I could arrange my schedule to fly to New York with him to become familiar with a new client.

Q And did you do that?

A Yes, I did.

Q As best you can remember,what happened when you flew to New York?

A Well,Mr. Natelli and I flew to New York to attend a meeting held between people at National Student Marketing and people of a potential acquisition company and the two

were presenting their side of the story hoping that they would eventually end up with a merger and Mr. Natelli and I went up as observers to just get a feel for the company.

Q Do you remember the names of any of the persons who were present at this particular meeting?

A I can remember Mr.Randall and Mr.Kelly. That is about all I can remember at that time.

Q That is Mr. Cort Randall, the son?

A Yes.

Q And that is Dennis Kelly, one of the account executives, is that right?

A Yes.

Q What is your next recollection of any event or anything happening with respect to the engagement of Peat, Marwick by National Student Marketing Corporation?

A About a day or two after that meeting I went over to NSMC offices to talk to Mr. Kurek to prepare to do the audit. It was preliminary discussions.

Q You are talking about, of course, Mr.Bernard Kurek, right?

A Yes, sir.

Q Had youever met him before in your life?

A No, I hadn't.

Q What was your understanding of his position with National Student Marketing Corporation?

A He was comptroller.

Q As you can best remember, who was present at this meeting that you had with him?

A He and I. There may have been Bill Chapman, but I am not sure.

Q Bill Chapman was a man who worked under Kurek at National Student Marketing?

A That's right.

Q As best you can remember, what was the conversation that you had with Kurek at that time?

A It was a normal-type of thing. We were there making arrangements for the audit, that is, asking the client when they would close their books, where we would work, if they had adding machines, things of that nature.

Q Directing your attention to the beginning of September of 1968, did the work begin by Peat, Marwick on this audit of National Student Marketing Corporation?

A Yes. We did -- we started during the first week of September.

Q You are aware, of course, that the fiscal year of National Student Marketing ended on August 31, 1968, is that correct?

A Yes.

Q Will you tell us what your experience had been up to that point with respect to when audit work started in relationship to the end of the fiscal year of a particular client?

A Generally the audit work would be done anywhere from a month to three months to six months after the client's year end.

Q Are there any reasons why that occurs?

A Yes. We have to wait until the books are closed, the client can make whatever adjustments they think should be made. Many times it takes weeks after the year end before the company can close its books. It is just a normal thing.

MR. STILLMAN: Can I have Exhibit 4C, please, Mr.Velie.

MR. VELIE: Yes.

MR. STILLMAN: So as not to disturb you again, if y ou can give me 3 and 2, I would appreciate it.

Q Mr.Scansaroli, what does Exhibit 4C represent?

A 4C is the general binder for the year ending 8/31/68. The general binder has the program, questionnaire and trial balance and maybe miscellaneous items.

Q I would like you to turn to Page 1499 of

Government Exhibit 4C. Do youhave that?

A Yes, I have.

Q That is the budget and time summary?

A Yes, sir.

Q What is that?

A Usually or normally before an audit is prepared we prepare a budget of the estimated hours that we are going to incur in making an audit and then as we are progressing through the audit we indicate on here the amount of time that we spend on the audit.

Q When you say "we" you are referring to whom, sir?

A Anyone that would have worked on the audit.

Q Do you then try to at some point add up the number of hours that are spent on a particular engagement?

A Yes, sir.

Q Does Exhibit 4C at Page 1499 reflect the total number of hours or the approximate total number of hours spent by personnel from Peat, Marwick on that particular engagement, namely, the audit of the August 31, 1968 financial statement of National Student Marketing Corporation?

A It shows 600 hours as of the end of October.

Q Who was working on this audit?

A There was myself, Mr. Natelli, Mr.Olderlander, Mr. Johnston, Mr.Britton.

Q The cumulative time of all of you gentlemen was approximately 600 hours?

A Through October,yes, sir.

Q Directing your attention, sir, to the early part of September of 1968, did you have occasion to go to the offices of the firm of Arthur Andersen & Company?

A Yes,sir.

Q Who is Arthur Andersen?

A Arthur Andersen were the former accountants, former auditors for National Student Marketing.

Q They were the persons who had done which audit for that company?

A For the year ended August 31, 1967.

Q Whom did you meet with when you went over there?

A I met with Ron Garwych.

Q Who was he?

A He was, I believe, the supervisor who handled thi engagement for Arthur Andersen & Company.

Q Was he basically your counterpart at Arthur Andersen?

A Yes, sir.

Q Without going into the conversation, did you and he discuss certain matters with respect to National Student Marketing Corporation?

A Yes, sir. We discussed the work papers in general.

Q Do you recall whether or not you received anything from him when you left that day?

A I did make Xerox copies of certain work papers. I believe I received Xerox copies of the fixed asset work papers. I am not sure. I may have also received a copy of the trial balance as of August 3, 1967.

Q In the period let's say during the month of September and going into October -- and you can look at Exhibit 1499 if you need any assistance -- who on behalf of Peat, Marwick, Mitchell was doing most of what I would call the day in-day out work, on behalf of Peat, Marwick?

A A great deal or most of the work was done by Mr. Oberlander with some done by -- also Mr. Johnston. Both of them were there on a daily basis.

Q What were you doing during this period of time insofar as this audit is concerned?

A Well,I was there working with them, I was there reviewing what they were doing, I was there answering questions. It is hard to say exactly what I was doing at that time.

Q Was one of the things that you were doing actuall reviewing some of the work papers which these men had pre-

pared?

A Yes, sir.

Q If you thumb through Exhibit 4C, for example, would wefind your initials at various places in the document?

A Yes, sir.

Q For example, there are some questionnaires which apparently were prepared -- bear with me a second.

I don't want to hold us up. Let me ask you to look at Page 1477.

A Yes, sir.

Q This is what is called a general questionnaire and pending matters and it is a document which has been filled out in part or perhaps in whole by yourself.

I see your initials.

MR. VELIE: Your Honor, I object to Mr. Stillman testifying.

MR. STILLMAN: Your Honor, I am reading from a document in evidence.

MR. VELIE: Then read it. You are saying he filled it out and all kinds of other things, Mr.Stillman.

MR. STILLMAN: Does your Honor sustain his objection to my question?

THE COURT: I hardly know what to say.

If you are reading from the document why don't

you read from the document.

MR. STILLMAN:All right, sir.

Ladies and gentlemen,this particular page I am looking at, Page 1477 -- of course,Mr.Scansaroli has the original up there -- you can see it is a general questionnaire and pending matters.

(Mr.Stillman read from Government Exhibit 4C in evidence to the jury.)

Q That was one of the things that you were responsible for doing in the course of that audit, is that right?

A Yes,sir.

Q Did there come a time in the course of this audit when Mr. Johnston was no longer working on it?

A Yes, sir.

Q Do you recall approximately when that was?

A I believe it was around the end -- third week or the end of September,September or October. I am not sure any more. During the middle of the audit at some point in time he was required to travel out of the country on another engagement.

Q Was another senior assigned to work on this engagement?

A No, sir.

Q Did anyone step in to do some of the work that Mr. Johnston had been doing?

A No one but me.

Q No one but you?

A Yes.

Q Precisely.

We heard a lot about these contracts in progress, Mr.Scansaroli, would you tell the ladies and gentlemen of

the jury, when you first had any conversation with anyone at National Student Marketing Corporation with respect to this matter?

A Either during the second or third week of October. We were working on the audit when at some point in time Mr.Randall, Mr. Kurek and I were talking together and Mr.Randall indicated to me that he had these contracts which were not the general ledger.

He indicated that they had recorded these contracts or part of these contracts in previous quarterly statements and that he thinks they should be on also as of August 31, 1968.

He explained to me why he thought they should be on the books as of 8/31/68.

Q Do you recall either the words or the substance of what he said when he told you why they should be on the books as of 8/31/68?

A In effect, he indicated that the people working on these contracts, the account execs, had worked all summer,and the actual contracts or commitments,what have you, would not be completed until some time during the school year, worked on until the school year and therefore, in order to match costs with revenues he thought it was

best to record these contracts as of August 31, 1968.

Q The work that was to be done in the school year, what, if anything, did he say with respect to what that work was?

A Well, the work that they had to do was the campus reps would put up posters on their campuses, they would -- I believe they would send out mailings to college and high school students some time after the school year started.

Q As of this point in time when you were having this conversation with Mr. Randall, had you given any consideration to whether or not National Student Marketing Corporation would show a profit or a loss for the period ended August 31, 1968?

A I did not focus on it at that time, no, sir.

Q Did it make any difference to you whether or not this company had a profit or a loss for the year ended August 31, 1968?

A No, sir.

Q Has it ever made a difference to you with respect to any client that you serviced while you were at Peat, Marwick, Mitchell with respect to whether or not that client showed a profit or a loss for a particular fiscal period?

A No, sir. We worked on so many companies, some would show a loss,some would show a profit.

As an accountant it doesn't make too much difference. Theyare just figures that you are working with.

Q What, if anything, happened after you had this conversation with Mr. Kurek and Mr. Randall with respect to the contracts in progress?

A I suggested that we talk to Mr. Natelli.

Q What was the reason for that suggestion?

A Because it was a type of accounting that I thought we should all discuss before we went ahead. Normally any type of decisions of that nature are not made by the supervisor unless they are first discussed with the partner.

Q That is true in all of the audit work that you had done on any other client than National Student Marketing Corporation?

A Yes, sir.

Q That is the way it is done, is that right?

A Yes, sir.

Q All right.

Did there come a time that you had any conversation with Mr. Natelli concerning this subject?

A I believe it was the same day, Mr. Natelli came over to NSMC's office and the four of us,Mr. Natelli, myself, Mr.Kurek and Mr.Randall were in Mr. Randall's office, and Mr.Randall again explained to Mr. Natelli exactly what he explained to me regarding the fixed fee contracts.

Q What, if anything, was said either by yourself or Mr. Natelli?

A I can't recall what we said at that point except that we had to think about it. We wanted to have a few hours to see -- to let us study it.

Q So that am I accurate then in saying that when you left on that occasion no decision had been reached with respect to what your or Mr. Natelli's views were on this particular matter?

A That's right.

Q Did there come a time thereafter, after you left the offices of National Student Marketing Corporation that day, when you and Mr. Natelli discussed this matter?

A Yes, sir.

Q Can you recall when? Was it a day, a week, the same day?

A It was either the same day -- I would think it was the same day. It could have been the next day. I believe it was that same afternoon.

Q All right.

As best you can remember now, Mr. Scansaroli, what was said between the two of you, either the words or the substance?

A We discussed the effect of recording the contracts and the effect of not recording the contracts and their reasons to record and their reasons not to record it.

After discussing the pros and cons, we thought that the way to -- the way the company was doing it in the previous three quarters was the correct way. The only change that Mr. Natelli suggested was that rather than record the complete contract, that we should record a portion of it by using percentage of completion.

Q What, if anything, happened after this conversation that you had with Mr. Natelli?

A Either that day or maybe a day later or two days later, again the four of us were standing together in Mr. Randall's office and Mr. Natelli indicated to Mr. Randall that we thought that the method used was proper but, however, we would like to confirm some of the accounts.

Q What, if anything, was said at that time by Mr. Randall or Mr. Kurek or anyone else?

A Mr. Randall said he didn't mind if we confirmed the accounts. However, he did not want us to confirm in

writing, if possible.

Q Did he tell --

A He would rather us satisfy ourselves by some other method.

Q What, if anything, else was said in the course of that conversation on this subject?

A We eventually agreed or he eventually agreed that he would see nothing wrong with us making telephone calls to the people involved with these contracts.

Q Do you recall whether Mr. Randall gave any reason as to why he would prefer that you not confirm in writing?

A He gave two reasons.

One, he indicated that the people in the advertising field were kind of fidgity people and didn't want to be bothered by auditors and, secondly, the way in which corporations signed contracts is that the process of getting a contract through a corporation is chain of command until it comes to a legal department is a long tedious process. He didn't want us to confirm them in writing because some of the people involved are not aware yet that this has gone through the chain of command yet and, therefore, he would prefer that we find out in some other way to satisfy ourselves that these were correct.

Q Will you tell the ladies and gentlemen of the jury

what your experience had been up to that date with respect to confirmations?

A Most cases in the past and just about every case I would say we had -- we would send written confirmations. Occasionally we would make a call or we would confirm something by using the telephone, but generally we would send written confirmations.

Q Would you tell us what your understanding was as of that time of what the purpose of the confirmation process was?

A A confirmation is to -- is made to satisfy the auditor that what the company said is on the books is correct.

Q By the way, at this point in time, did you know that substantially all of these commitments that you had been told about were oral commitments?

A Yes, sir.

Q All right.

Did Mr. Natelli give you any instructions or did you have any conversations with him with respect to how you should then proceed?

A Yes, sir.

Mr. Natelli suggested or directed that I fly to New York with a schedule that was prepared by the client on

these contracts.

He suggested that I fly to New York, talk to the account execs who were responsible for the contracts, review correspondence files and make the necessary phone calls to satisfy myself that those commitments were proper.

Q Did you receive any instructions with respect to anything that should or should not be in your work papers?

A No, sir.

Q What happened? What did you do, if anything?

A I did exactly that. I flew to New York. When I got to New York I was given an office, an office of someon that was out of town, and that was my more or less base of operations for that day.

From there I made some telephone calls. I reviewe the correspondence file. I also made some of the phone calls I believe from the offices of the account executives.

At certain points they placed a call and at some points I placed a call. Several confirmations I could not make becaus e the people that I was calling were not in. Therefore, when I got back to Washington the next day I made some of the calls from Washington.

THE COURT: Forgive me, Mr. Stillman, for interrupting.

Mr. Scansaroli, is it correct that prior to these

conversations that you have been telling us about with Natelli, Randall and Kurek, NSMC and its previous auditors, Arthur Andersen and Company, had not been working with a percentage of completion method?

THE WITNESS: No, sir, they were using the contract method, but they would record the entire contract rather than percentage of that contract.

THE COURT: Right. So that the change which you have told us that Natelli finally suggested to you and to Randall and Kurek came right in this area, that you were going to record the contracts, but you were only going to record percentage of completions and so on?

THE WITNESS: Yes, sir, if you call that a change I'm not so sure that's a change. It is a fine point there. There is a change from recording the complete contract to recording percentage of completion, that is right.

THE COURT: I believe you used the word "change".

A Okay, I believe that's right.

THE COURT: All right. I just wanted to clear it up so that we could understand it.

Thank you.

Q Would you look at Exhibit 3, Mr. Scansaroli. Would you tell the ladies and gentlemen of the jury what Exhibit 3 is?

A Exhibit 3 are the special sales working papers for the year ended August 31, 1968.

Q Starting with the cover of that document, is that your writing?

A Yes, sir.

Q We then turn to the first few pages, that is, 1911 through 1914.

Is that also in your handwriting?

A Yes, sir.

Q What do pages 1911 through 1914 represent?

A These work papers represent the discussions that Mr. Natelli and I had and also represent the discussions between the personnel at National Student Marketing Corporation regarding the type of contracts that the company was recording and the reasons for the alternative methods that we had to record these contracts.

Q Did you write these first four pages of this document?

A Yes, sir.

Q Did you write them on or about the 26th of October 1968?

A Yes, sir.

Q Who asked you to write this up?

A Mr. Natelli.

Q Did you then put this into the work papers, Government's Exhibit 3?

A Yes, sir.

MR.STILLMAN: Your Honor, I would like to take a moment or two and read this to the jury now, if I might.

THE COURT: All right.

MR. STILLMAN: Thank you. The heading of this first page, ladies and gentlemen, is "National Student Marketing Corporation."

Then we have SP-1, the initials JS, Joseph Scansaroli, the date October 26, 1968, "Method of Recording Gross Income."

Here it is in its original form, Mr. Foreman, ladies and gentlemen.

Q This is it as you write it back then, is that right, Mr. Scansaroli?

A Yes, sir.

Q In pencil?

A Yes, sir.

(Mr. Stillman read from Government's Exhibit 3 in evidence.)

Q Did you write that, sir?

A Yes, sir.

Q Was it an expression of your best professional judgment at that time?

A Yes, sir.

THE COURT: May I ask you in this connection, Mr. Scansaroli, is it fair to say that one of the concerns that you were expressing or at least suggesting there was that usage of the completed contract method of accounting would create a sort of peaks and valleys financial picture over a period of time?

THE WITNESS: Yes, sir.

THE COURT: Whereas in comparison to that a percentage of completion method would allow the company to show a steady or continued progress as work was going along and being completed.

THE WITNESS: Yes, sir, that is the reason behind it.

THE COURT: That is, I believe, one of the reasons why people in your profession oftentimes use percentage of completion for firms which have contracts or jobs which take a long time to complete?

THE WITNESS: That's right, yes, sir.

THE COURT: On the other hand, would it not be

fair to say from your professional viewpoint that in order for percentage of completion method of accounting to work that pre-supposes complete and accurate records of work in progress and accounting or financial records relating to each one of the contracts or deals?

THE WITNESS: Yes, sir.

THE COURT: And absent those data the percentage of completion method becomes somewhat chancy and ineffective from an accounting point of view?

Is that a fair statement?

THE WITNESS: Yes, sir.

THE COURT: Forgive me, Mr. Stillman.

MR. STILLMAN: That's all right, your Honor.

Q The fact of the matter is, as reflected in Judge Tyler's questions, that was the problem which confronted you in the fall or the late summer or early fall of 1968, isn't that right?

A That's right, yes.

Q I believe that this document reflects -- is it a fact that the records that the client had at that point were not in the best shape?

A That's right, yes.

Q The fact is that the client did tell you that the agreements were basically oral, is that correct?

A Yes, sir.

Q Nevertheless, that was the situation which confronted you as professionals at that period of time, is that right?

MR. VELIE: Objection to the leading and repetitious and argumentative.

THE COURT: Sustained as to form.

Q Knowing of the facts that we have just talked about did you then proceed to make a decision?

A Yes, sir.

Q What was the decision that you made?

A We made the decision to record the contracts on a percentage of completion basis.

Q And at the time that you made that decision, did you make it in good faith?

A Yes, sir.

Q What was the purpose of writing up the summary that appears in the first four pages of Government's Exhibit 3?

A So that if anyone had any questions regarding our decision, the method that we were using or why we did it, they could look at the work paper and determine why.

THE COURT: As I understand it, you did that at the direction of Natelli?

THE WITNESS: Yes, Your Honor.

Q Did you also have occasion to write up in Exhibit 3 the nature of the audit procedures which you followed in doing this work? I direct your attention to page 1970.

A Yes, sir.

Q What does this page represent?

A This page basically indicates what we did with regard to these contracts. It tells the people who we talked to on what contracts. In addition it indicates that so many of the contracts were signed contracts. In effect, it is a summarization of what we did.

Q You used the term "we". Who is the "we"?

A Well, I did this, I made this summary.

Q This is your work, right?

A Yes, sir.

Q In your hand, correct?

A Yes, sir.

Q With your initials on it, right?

A Yes, sir.

MR. STILLMAN: I would like to read Page 1970 and also 71, your Honor. I will give Mr. Velie my copy.

Actually, believe it or not, the Xerox reads easier than the original. So I am going to take advantage of him and take the copy.

Mr. Foreman and ladies and gentlemen, Page 1970 is headed "National Student Marketing Corporation, Audit Procedures, August 31, 1968," which is the date of the audit, is that right, sir?

THE WITNESS: Yes, sir.

MR. STILLMAN: SF7, the initials of Joseph SCansaroli, the date October 23, 1968.

(Mr.Stillman read from Government Exhibit 3 in evidence to the jury.)

Q Again, of course, the "we" is you,sir, right?

A Yes.

MR. STILLMAN: Mr.Foreman and ladies and gentlemen, just to show you how this is structured and what I am reading, I am going to read the information and you will see on the far side there are the numbers, so it is a kind of a schedule of sorts.

I am sorry. Did you all see that? I didn't mean to walk too quickly.

(Mr.Stillman read from Government Exhibit 3

in evidence to the jury.)

Q That last entry, Mr. Scansaroli, I gather refers to physical documents which you saw?

A Yes. They were either commitment letters or contracts or some type of written documentation.

Q Does this note reflect then that so far as you were concerned these are the persons that you talked to in doing this work at that time?

A Yes,sir.

MR. STILLMAN: The next page. Actually, it has a different title. It is headed "Accounting Procedures."

Q Would you look at this page, which is 1971, Mr. Velie, and tell us what that page represents.

A It indicates what Mr.Kurek was going to do once this method was adopted.

Q Had anybody told Mr. Kurek or advised Mr. Kurek as to what it is he should be doing?

A Yes, sir.

Q Who is that?

A Mr. Natelli and myself.

MR. STILLMAN: The next page, Mr.Foreman and ladies and gentlemen, again, "National Student Marketing Corporation," this one headed "Accounting Procedures, 8/31/68," and the date of this is October 23, 1968.

Q This, of course, is in your handwriting again, Mr. Scansaroli?

A Yes, sir.

(Mr. Stillman read from Government Exhibit 3 in evidence to the jury.)

Q Mr.Scansaroli, would you turn please to Page 1916 of Government Exhibit 3 and tell the ladies and gentlemen of the jury what that page represents.

A This is a schedule of contracts in progress as of 8/31/68. It shows the client, the amount of the contract, the cost of the contract and the percentage of completion.

Q I notice that there are, at least as shown up on my Xerox, checkmarks and other notations. What are those?

A Those checkmarks indicate what I did with regard to each individual contract.

Q Will you tell the ladies and gentlemen of the jury how this is structured, that is, what the checkmarks represent?

A Well, the checkmarks are in color and there are different types of checkmarks. There are checkmarks plus there are checkmarks with crosses in them.

There is a red checkmark, which indicates that

I talked to the personnel of the companies involved, "See memos attached," and the green checkmark that says "talked to ad agency responsible for advertising for client company," there is a red checkmark with a cross that says "examined signed contract," there is a blue checkmark -- I take that back -- I think that is a green checkmark with a cross that says "examined letter of commitment," and on top of these checkmarks there is a blue checkmark that says "cost computed based on estimate per work paper 4-2."

What would accountants do without checkmarks.

MR. STILLMAN: May I, your Honor, just show it to the jury, please.

THE COURT: Surely.

MR. STILLMAN: Mr. Foreman and ladies and gentlemen, I thinkit speaks for itself. I hope you all can see it. I will move down the row.

(Pause.)

THE COURT: Incidentally, Mr.Scansaroli, in this period of time,that is to say, late September, October of 1968, did you have occasion to evaluate how long these oral contracts were going to take to complete, assuming they went along according to plan, were finalized, and all the rest?

THE WITNESS: We didn't make an evaluation, no,

sir. We were under the impression that the contracts would be completed some time in the spring -- either the fall or the spring of 19 -- the spring of 1969, possibly even the fall of 1969.

THE COURT: In other words, they might take less than a year or perhaps they might take a year or even a little more?

THE WITNESS: Yes, sir.

THE COURT: But that was an impression?

THE WITNESS: Yes, sir.

THE COURT: Kurek or Randall, were they ever asked by you or, to your knowledge, by Natelli about this?

THE WITNESS: I believe they expressed this to us. I don't recall any specific conversation, no, sir.

THE COURT: All right, sir.

MR. STILLMAN: Would this be an appropriate time?

THE COURT: Yes, I think that is a good idea. We will take the morning recess at this time, ladies and gentlemen. Ten minutes.

(Recess.)

(In open court; jury present.)

Q Mr.Scansaroli, Judge Tyler asked you about these programs.

Were you made aware of any distinction between the time when the larger programs would be put into effect as to be distinguished from the smaller ones?

A Yes. Usually the smaller programs were for the next semester. These would be for the period around December, January, December of '68, January of '69. There may be some programs that went six months later. It depends on a contract. There could be somewhere a contract was large enough that the programs would be over a period of time.

MR. VELIE: Excuse me. Mr.Scansaroli, when a lawyer stands up, it is to object. Please, if you would, stop answering.

Your Honor, I asked him --

MR. STILLMAN: Your Honor --

MR. VELIE: I would like to have that done again and stricken as unresponsive. He was asked if he was made aware. I would like to know who made him aware and when.

THE COURT: That is not an objection. That is not an objection at all. It can be clarified. Perhaps

Mr. Stillman will do it for you or you can do it on cross.

MR. VELIE: Very well.

THE COURT: That certainly is not an objection. Go ahead, Mr.Stillman.

Q How did you learn of this, Mr. Scansaroli?

A Just by association with the company and the personnel within the company.

Q Such as whom?

A No one told me directly that I can recall, but just by being there on a daily basis and by talking to people you could see what is happening.

Q Who were the kinds of people -- can you give us some examples if you can remember of the people you were talking to?

A Bill Chapman, who was -- who handled the contrac at that time, Bernie Kurek, Cort Randall, the account executive.

Q I would like to turn our attentionto the matter of the costs of some of these programs. I would first like to direct your attention to Page 1919.

Will youtell the ladies and gentlemen of the jury what that page represents?

A This page represents the cost of -- this page

represents the cost to NSMC client for inclusion in what they call the collage mailing. This page shows for every thousand mailings it would cost $87. Twelve companies would have inserts in this mailing, which was a large envelope, and each company's cost would be $7.25 per thousand. It also indicates that commissions are paid to the account execs and to the student representatives based on poster waves. For every set amount of posters, these people would get a set commission.

Q Couldyou turn to Page 1920 and tell us what that page represents?

A This page represents the gross contract plus cost and commissions of one brand for the Clairol contract.

Q And the Clairol indicates on here that this company is committed for $500,000?

A Yes, sir.

Q Would you look at page -- I am not sure which page it is. Did there come a time that you learned there was some error made by you in the booking of the Clairol contract insofar as its amount is concerned?

A Yes, sir.

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Q Can you tell us what that error was?

A We made an error in totalling the cost on the Clairol contract with the result that the gross profitabilit was in error.

Q And it was an error by an upward amount of about $67,000?

A Yes, sir.

Q When did you learn that for the first time, Mr. Scansaroli?

A I learned about that error about four to six week ago when I was reviewing the work papers with you.

Q Would you look at page 1976.

What does that page represent?

A This page is the listing of the contracts as of 8-31-1968, I believe prepared by Mr. Kurek.

Q Would you look on the reverse side, and I see som writing on there.

What is that?

A These are notes that I made to myself as I was talking to the people confirming these contracts.

Q In other words, back in October of '68, jottings that you made right on this particular work paper?

A Yes, sir.

Q If you would now turn to 1983 and tell us what

those sheets of yellow paper represent?

A These again are scratch notes that I was making as I was talking to various people on the telephone.

Q And you took those notes and bound them up in this set of work papers when you put them together?

A Yes, sir.

Q Turn back to 1970.

A Yes, sir.

Q The entries for Gossard and Chicken Delight, the name of Frank Salgan and I. S. Berlin, at the time you made this note, whom did you believe Frank Salgan to be?

A I thought they were an ad agency.

Q Did you generally learn that I. S. Berlin was, in fact, the company which did the bulk of printing work for National Student Marketing Corporation?

A Yes, sir.

Q At the time that you learned that they were the printer, did you put together the fact that you had talked to him before believing him to be the ad agency?

MR. VELIE: I object to leading in this fashion, your Honor.

THE COURT: I agree, Mr. Stillman. Perhaps you are intending to expedite, but I think you better not.

MR. STILLMAN: All right, your Honor.

Q Do you remember when it was that you learned that I. S. Berlin was doing a substantial amount of the printing work for this company?

A I believe it was during 1969 sometime.

Q At the time that you learned that, did you consider the fact that you had made this notation in your work papers back in October of 1968?

A No, sir. The first time I learned about the fact that this notation was made was at the time that I was testifying before the SEC.

Q Would you turn to the forth part again of Government's Exhibit 3 and turn to page 1912. I read to the jury before the paragraph that begins on that page, "The only other feasible way".

Do you have that before you?

A Yes, sir.

Q The second sentence reads, "Under this method extreme caution should be used because there is no legal binding contract."

Would you explain to the ladies and gentlemen of the jury what you meant by that entry?

A I mean first of all there was no written document, and because there was no written document we were trying to get over the fact that the client must keep better

records. They must keep proper records working up to the point that they would have a signed document.

Q Doing the workthat you now outlined for us as reflected in Government's Exhibit 3, at the time you did this work, did you have in mind anything other than to do a fair and proper job for this client?

A No, sir.

Q I would like to now direct your attention to December of 1968. You will recall that there has been some testimony here with respect to a meeting. I believe Mr. Kurek and Mr. Buck testified about a meeting at which certain things were discussed. Do you recall that meeting?

A I recall it in general terms, yes, sir.

Q Would you tell the ladies and gentlemen of the jury, first, do you recall it having occurred sometime in December of 1968?

A Yes, sir.

Q What is your best recollection of what occurred at the meeting? If you could first perhaps tell us whom you recall having been there.

A I believe that Mr. Natelli and myself and Mr. Kurek, John Buck, and I believe Mr. Chapman was at this meeting.

Q What is your best recollection of what transpired?

A This was in effect one of the follow up meetings that we had after we completed the audit where we were discussing the type of documentation that the client or the accounting department should obtain from the account execs and basically I can recall designing some type of form that would go out to the account execs. That is about all I can remember about it.

Q The purpose of these forms was to do what, sir?

A To record these contracts and keep a record on a monthly basis and sometimes on a weekly basis.

Q What was the purpose of having that information, if it was expressed at that meeting?

A Well, the purpose was to ascertain what the percentage of completion would be as they were going along. This in effect would help them when they prepared their quarterly reports and would also give them some historical data for future years.

Q I would like to ask you to focus your attention, Mr. Scansaroli, on a period of time, namely, the period of time between December of 1968 and April or May of 1969.

During that period of time were you engaged in doing accounting work for other clients of Peat, Marwick?

A Yes, sir.

Q Was a Vim Company one of those clients?

A Yes, sir.

Q And this company you told us about before, Stedman Securities?

A Yes.

Q And the D. C. Transit Company.

A Yes.

Q In that period of time that we have now talked

about what is your best recollectionof what, if anything, you were doing with respect to National Student Marketing Corporation?

A About the only thing that I can recall doing between basically the audit of '68 and working on the proxy in '69 was reviewing several acquisition agreements that NSMC had forwarded to our office.

Q In that period of time, did you attend any of the Saturday sessions that Mr. Kurek testified he had with Mr. Cort Randall?

A No, sir.

Q Did you have any knowledge of those sessions?

A No, sir.

Q Did you attend during that period of time any Finance Committee meetings of National Student Marketing Corporation?

A No.

Q What is your best recollection of your first awareness of the proxy statement which was to be prepared fo National Student Marketing Corporation in 1969?

A I can't recall when I first became aware that we were going to work on this proxy statement. The only thing I can say is that we did work on it in May and it would have had to have been sometime between February and May.

Q In the course of that work, were you called upon to do any review of the company financial statement for the period ended February 28, 1969?

A Yes, sir.

Q Will you tell us as best you can recall the nature of the work that you were doing with respect to that financial period?

A The period that we were using was what we call a stub period. It was the period from August 31, 1968 to February 28, 1969. These were unaudited figures and when unaudited figures are included in a proxy statement in this manner the accountants are required to make a limited review to ascertain if there is anything unusual that happened between August 31 and February 28.

We did this through a preprinted program that the firm had which we used.

Q In this period in the Spring of 1969, therefore, you were working on, wereyou not -- this is somewhat repetitious; I just want to establish this -- you were working on the proxy based on its including the February 28, 1969 figures, is that right?

A That's right.

Q Did there come a point in time when a decision was made by the client not to go forward with the proxy, includ-

ing the February 28, 1969 figures?

A That's right.

Q In your mind when do you best recall that having occurred?

A I believe it was sometime in May '69.

Q Just jumping ahead for a moment to establish where we are at, did there come a point in time when you later learned that the company was to go forward with a proxy statement this time based on its figures for the perio ended May 31, 1969?

A Yes.

Q Approximately when did you learn of that?

A I can't really say. It could be anywhere during the summer.

Q During the summer of '69?

A Yes, sir.

Q It is that work which leads to the events in August of 1969, is that correct, sir?

A That's correct.

MR. STILLMAN: May I have Exhibit 13, Mr. Velie, please.

Q Would you look at Exhibit 13 in evidence, Mr. Scansaroli, and tell us what it represents?

A This represents the work papers that were pre-

pared by the accounting firm, Peat, Marwick, Mitchell, and work papers prepared by the client for the proxy statement as of February 28, 1969 and as of May 31, 1969.

Q Would you look at the cover page of that document. Is that in your writing?

A No, I believe it is not.

Q I would like you to turn to what I believe is page 2520. Do you have that?

A Yes.

Q What does that page represent?

A This represents the original batch of papers for the February 28 proxy statement which we bound up in one batch.

Q In other words, Exhibit 13 consists of the work papers for the work done based on the February 28, 1969 figures, is that right?

A Yes, sir.

Q And it is supplemented by the work done for the period ended May 31, 1969, is that correct?

A Yes.

Q What is page 2521 of Government's Exhibit 13?

A This is an index of all the working papers that was prepared for the period ending February 28, 1969.

Q Who prepared that index?

A I did.

Q Do your initials appear thereon?

A Yes.

Q And the date on or about which you prepared it?

A Yes.

Q What is that date?

A May 23, 1969.

Q The numbers in red are what, sir?

A Those are the work papers where one can find what is described on the lefthand side of that work paper.

MR. STILLMAN: May I just exhibit this to the ju your Honor.

Q Do you recall, Mr.Scansaroli, when it was that you put together that portion of this binder which relates to the index that appears at Page 2521?

A This was put together around the end of May some time.

Q When you put together a set of work papers like that what was the practice at that time as to what was done with them physically?

A We would put them -- we had a separate room where we would file our work papers in alphabetical order.

Q By client?

A By client.

Q Who had access to that room?

A Anybody in the office.

Q Would you turn to Page 2617 of Government Exhibit 13. Will you tell us, Mr.Scansaroli, what that page represents?

A Yes. There is two pieces of paper that was prepared by the client showing the unbilled receivables as of November 1968 and as of February 28, 1969.

Q You say two schedules. You are referring to the schedule appearing at Page 2618, is that right?

A That's right, yes.

Q Can you tell us what if anything you did with

respect to those schedules?

A I took the schedules and I went over each item with Mr. Kurek and possibly Bill Chapman and I indicated on the paper my comments oneach -- on the contracts. Not on every one, but the majority of them.

Q Now would you turn to Page 2622, Mr.Scansaroli. What does that page represent?

A These are questions that I had raised during this period of time and my answers to these questions.

MR. STILLMAN: This is the page that I believe Mr. Velie read to us earlier in the trial.

(Mr.Stillman read from Government Exhibit 13 in evidence to the jury.)

Q Do you recall that?

A Yes.

Q By the way, there is a name that appears at the top which looks something like Lloyd Poplin. Do you have any recollection as to who that was?

A No, sir, I don't.

Q It is a notation you made back then?

A Yes,sir.

Q Would youturnto Page 2623 and also to 2624 and tell the ladies and gentlemen of the jury what those pages

represent.

A These are -- the first page is the letter that was received by the client from the Pontiac division of General Motors and the second page is the estimated budget for this program.

Q On this second page, 2624, are there any notations in your handwriting?

A Yes, sir.

Q This particular page is headed what, sir?

A "Analysis of Pontiac contract."

Q And then stapled to your page is a document headed what, sir?

A "Pontiac Marketing Plan, Youth Market, Budget Recap."

Q From whom did you obtain these documents?

A We obtained it from somebody at NSMC, but I don't know which individual.

Q Do you recall whether or not during that period of time there was any discussion between either yourself or Mr. Natelli and anyone at National Student Marketing Corporation with respect to this Pontiac letter appearing at Page 2623?

A Yes,sir. Mr. Natelli received a copy of this letter. He showed it to me and he indicated that the letter

was not definite and therefore he could not accept the letter as it was.

He indicated to Mr. Randall and Mr. Kurek that they would have to get better documentation for this contract, otherwise they would have to delete it from the proxy statement.

MR. VELIE: Mr.Reporter, if there is a date given in the preceding answer, would you read it to me?

MR. STILLMAN: Mr.Velie, I will take care of it. Just be patient.

MR. VELIE: Fine.

Q What is your best recollection of when this conversation takes place?

A This was at some point in time when we were preparing the proxy statement for February. I don't recall what date it was.

Q This particular work paper and, indeed, many of the work papers that pertain to this work seem to be dated on May 22, 1969. Did you do all of the work on that one day?

A No,sir. We, specially me, I had a bad habit of initialing the work paper at the time that I stapled this letter down on the work paper. We could very easily have received this letter two months or -- I mean, two weeks,

three weeks, a month in advance. But the date on the paper is usually the date that this letter is stapled to that paper.

Q In connection with the proxy statement based on the February 28, 1969 figures, were you engaged in doing anything other than work with respect to the contracts in progress for NationalStudent Marketing Corporation?

A Yes, sir.

Q Will you outline for the ladies and gentlemen of the jury some of the other things that you were looking at for this particular financial period, and if you need to, refer to the work papers to refresh your memory on that.

A In order to prepare all of the financial statements that went into the proxy statement it was necessary to prepare consolidating trial balances for the five years ended August 31, 1968, plus the stub period. In order to do that we had to get the information from our other offices for each one of these companies. This information was sent to us in Washington and we would take these figures and prepare these consolidations and come up with the final financial statements.

This was, I would say, the major task in this whole job of preparing this proxy statement.

Q By way of illustration, Mr. Scansaroli, would you

turn to Page 2522 of Government Exhibit 13 and tell us what that page represents, that page and the pages that come after it.

A Okay. These are the -- these figures here are the trial balances as of 8/31 -- this one is at 8/31/65, then it goes to 8/31/68, 8/31/67, and so on.

And what they are is taking -- we had to go back to 1966 with companies that were acquired in 1968, These companies had to be reflected back into 1966 figures. Therefore we had to prepare a trial balance using the original National Student Marketing figures plus all the acquisitions made since that date, and this was the major task of putting this proxy statement together.

Q For example, at 2552 I see some financial statements.

Whose are those?

A This is a statement for what is New Sportswear, Inc., as of December 31, 1968. It is a certified statement prepared by-- certified to by another accounting firm.

Q Did you do any work with respect to that particular set of statements? And I direct your attention to 2552 and the pages that come after.

A It indicates that we had to break out certain expenses that the -- that these accountants had lumped into one figure to meet SEC requirements.

Q You say "we."

Who was doing that work?

A It could have been me, Mr.Oberlander and several other people that were working with me.

Q Turn to Page 2566, if you would, and the pages that come after that. What is reflected there?

A This is the financial statement of International Study Services,Inc., as of October 31, 1968, certified to by ArnoldBerman & Company.

Q At the top of that particular page, 2566, it says "Report of N.E.T." Is that New England Travel?

A That's right.

Q By the way, with respect to Mr.Berman, you heard his testimony, did you not?

A Yes,sir.

Q Did you recognize him?

A I did not recognize him.

Q Do you recall the incident?

A No,sir, I don't.

Q Would you turn to Page 2593, Mr.Scansaroli. Do you have that 2593?

A Yes,sir.

Q What does that page represent, that and the next page?

A This is a program that we were to perform. These indicate the steps that we were to perform during our examination of unaudited figures.

Q And the examination was for what period of time?

A February 28, 1969.

Q Do anyone's initials appear on this document?

A They are my initials.

Q Can you tell us who performed the review reflected in pages 2595 and 2594?

A I did.

Q This is the document, if I might just read the heading.

"Outline for review of interim unaudited financial statements included in registration statement at subsequent period to effective or closing date."

What is your best recollection, Mr.Scansaroli, of when you first heard of the matter of the writeoff of the RonMichaels contracts?

A Some time during the period that we were preparing the proxy statements for February 28.

Q Who did you learn that from?

THE COURT: Excuse me. Would that mean, as you recall it, some time between February and May?

THE WITNESS: Yes, your Honor.

Q You said between February and May.

Did you start this proxy work in February, as best you can remember?

A I don't recall. It had to be in that period of time.

Q All right.

You pick May because that is the date that appears on most of the work papers, is that right?

A Yes,sir.

Q If not all of them. I believe you started to tell us from whom you learned about this matter of the Michaels contracts.

A Mr. Natelli informed me.

Q Was anyone else present when you discussed the matter with him initially?

A I can't recall, no, sir.

Q All right.

What is your best recollection of what you were told?

A Mr. Natelli indicated to me that Mr. Randall had informed him that Ron Michaels had taken kickbacks and therefore those contracts were no good.

Q Was there any discussion as to what, if anything, had to be done with respect to those contracts?

A I can't recall any specific instruction except that they had to be written off.

Q Was there any discussion as to whether they would be written off to the current period or to any other period?

A It was -- it was decided to write them off for the year ending August 31, 1968.

Q How was that decision arrived at?

A It was arrived at basically by the fact that it was a contract that should never have been in existence as of 8/31/68 and based on Opinion 9, that we could ascertain the contract should have been written off retroactively.

Q Would you look at Page 2531 of Government Exhibit 13.

Who made the entries on 2531 and 2532?

A I did.

Q With respect to those on 2531, what is your best recollection of when those were made?

A Here again it was some time in May. I dated the work paper May 12. I am sure it was in that period of time.

Q There's been a great deal of testimony concerning those entries, Mr. Scansaroli. You are the man that wrote them.

Will you tell us what they are and what you meant to convey by them?

A Yes, sir. These entries -- the first two entries on this page where we are writing off the accrued cost and sales and the cost of sales and the accrued liability and the deferred taxes, these two entries were combining entries.

We could have, or I could have made three separate entries, but being in a hurry, not thinking about any other reason, I made a combining entry. It is a thing that the accounting people do every day of their lives. There's nothing unusual about making a combining entry such as this.

The reason the tax is made in this manner, I would like to explain that, too.

When an accountant prepares a provision for taxes, it is generally an estimated figure, it is not an exact figure. An exact figure for taxes cannot be determined until the tax return is prepared. When accountants are doing an audit, they prepare a provision for taxes to the best of their ability, but they are not tax people and there could be tax technicalities that they are not aware of which will

change the final result. What accountants do, they more or less round off the figure.

If, for example, I decided I would have a tax liability, I compute it on my work paper of $235,300. I can round that off to $300,000. This, in effect, provides a cushion for any adjustment that may occur after the tax return is filed. Whenever I made this adjustment, although the tax could have adjusted by 109,000, I decided let's adjust it to 188,000 and leave the rest as a cushion in the tax liability account.

That is exactly why this is to the penny, as Mr. Velie keeps saying, because for that reason.

Q Did you make that entry to conceal anything from anybody?

A No, sir.

Q Do you know Carol Raimondo?

A Yes, sir.

Q She was at Peat, Marwick as she testified during the same period of time when you were there?

A Yes.

Q The fact of the matter is that the two of you learned you had passed your CPA exam at the same time, is that correct?

A That's right.

Q Do you recall the conversation with Carol concerning the tax adjustment that she was discussing with you?

A In general I do. We were discussing -- I can recall discussing the tax effect of this with Carol and Gene Holloway and Mr. Natelli, and the general conclusion was that the tax provision as of 8-31-68 was incorrect, it should have been no tax provision at all.

Q Do you recall the exhibit which Mr. Martin showed to Mr. Buck when he testified with respect to the journal entries that you prepared?

A I'm not sure I understand which one they are.

MR. STILLMAN: It's been previously marked, your Honor, as Natelli Exhibit M for identification.

Q Is it a fact, Mr. Scansaroli, that if you wanted you could have made the entries as they are reflected on Natelli Exhibit M for identification?

A Yes, sir.

Q In other words, you could have combined ~~convinced~~ the entries to show the retained earnings items with respect to journal entries one and two appearing at page 2531, is that right?

A That's right.

Q And all that you did -- and Mr. Martin demonstrated this earlier on Mr. Buck's testimony -- was to com-

bine the entries to facilitate the matter, is that right?

A That's right.

Q Alongside of it is the first portion of an entry which you made back on May 12, 1969, is that right?

A That's right.

Q Did you have anything criminal in mind when you made that entry?

A No, sir.

MR. STILLMAN: I would like to offer that in evidence, your Honor.

MR. MARTIN: I have no objection, your Honor.

MR. VELIE: I think the jury has seen it twice. We might as well let it in.

No objection.

xx (Defendant Natelli Exhibit M for identification, received in evidence.)

Q Turn to page 2532, Mr. Scansaroli.

Tell us what that entry reflects?

A That is the entry writing off the Listerine contract.

Q At the bottom of that entry appears "To adjust Listerine contract, explanation on journal entry number 2."

Do you see that?

A Yes, sir.

Q What is the explanation that that refers to?

A That refers to the write off of the Ron Michaels contracts.

Q What do you say in your work papers with respect to that write off ?

A On the Ron Michaels contracts I said, "Based on subsequent facts it was decided to adjust three contracts entered into by Ron Michaels, Clairol, Cheeseborough and Ban. This, in effect is, the same as a reclassification entry for report purposes."

Q Now, in making these entries that appear on your work papers, did you feel in any way that you were somehow exposed to some work that you had done in connection with the 1968 audit of National Student Marketing Corporation?

A No, sir.

Q Have you ever felt that?

A No, sir.

Q I would like to direct your attention, sir, to August of 1969.

Did there come a time when you saw a draft of the proxy statement?

A Yes, sir.

Q Mr. Scansaroli, I have layed before you what has been marked as Government's Exhibit 17, which is a draft of

the proxy, approximately August 9, 1969.

Do you recall seeing a draft of the proxy statement at or about that time?

A Yes, sir.

Q In what connection did you see the draft?

A I don't think I understand the question.

Q I'm sorry.

How did it come about that you saw a copy of the draft of the proxy statement?

A Because I was the supervisor and I would review the draft as it came back to see if I saw any errors or corrections that should be made.

Q This document is filed with financial information, is it not?

A Yes, sir.

Q Was any of the financial information that appears in this document your responsibility?

A Yes, sir.

Q What part of it was your responsibility?

A Quite a bit of it, sir.

Q Who was supposed to review the figures and put them together as they came in from the various subsidiaries of National Student Marketing Corporation?

A It was my responsibility to make sure it was done.

Q That entail any great amount of work on your part?

A Yes. It was -- like I said, that was the major task in this proxy statement, and two, three, maybe four of us were doing this work. It took us several weeks.

Q Let's turn to this footnote. Would you look at Exhibit 8, which is in front of you. That is that spread sheet.

I am sorry. I got the number wrong.

THE COURT: Let's get that number right.

MR. VELIE: 17B.

MR. STILLMAN: Maybe I will put the big one up. Does everybody have a clear view of that?

Q The lefthand side of the sheet is the draft of the footnote on August 5, 1969. Do you identify it as such, sir?

A Yes.

Q The middle column is the draft with the notations on it by Mr. Natelli.

A Yes.

Q The last is the final as it appears in the proxy statement?

A Yes.

Q Were you aware, sir, that a change was made from

the draft as it appeared on the first part of this exhibit to the language as it appears in the center portion?

A I can't recall.

Q Do you recall whether or not you had any discussions with Mr. Natelli concerning the change that was made?

A I can't recall if we discussed the change or not. I know we discussed the original note and I believe that he may have discussed it with me. I don't recall.

THE COURT: When you say "the original note" which note do you refer to, sir?

THE WITNESS: On the first draft.

THE COURT: Are you talking, for example, about note C?

MR. STILLMAN: I am sorry, your Honor. Perhaps I have not been clear enough. We are referring to note C and note E as they appear in the first column of this particular exhibit.

THE COURT: I understand that, but I want to make sure that the witness understands it too.

MR. STILLMAN: Very well, I appreciate that, your Honor.

THE WITNESS: Yes. We discussed both notes. Before this was ever done we discussed the method that this

type of thing would be disclosed in the financial statements.

THE COURT: When you say "we" I assume you refer to yourself and Mr. Natelli?

THE WITNESS: Mr. Natelli, yes, your Honor.

Q Did you become aware of that fact or did you learn that the change was made as reflected in the center portion of this exhibit?

A I became aware of it eventually, yes.

Q You are aware that in its final form it appears as it is in the last portion of this particular exhibit, Government's Exhibit 65-10?

A Yes.

Q Do you know who Mr. Lee Otkiss is?

A Yes.

Q Who is he?

A He is a partner in the Philadelphia office of Peat, Marwick, Mitchell.

Q Do you know whether or not he had any responsibilities with respect to the proxy statement for National Student Marketing Corporation?

A Yes. He was the SEC reviewing partner with regards to this client.

Q What was your understanding then of the role of

the SEC reviewing partner?

A Well, prior to submitting anything to the SEC with Peat, Marwick's name on it it was his job to review the statements to see if there was anything unusual or anything that wasn't meeting or wasn't in conformity with SEC requirements.

Q So far as you knew, he was going to be performing that work with respect to this very proxy statement, the final of which is Government's Exhibit 25 in evidence?

A Yes.

Q To the best of your knowledge, was the change made from the draft as it appears in the first column, as reflected being done in the second, and coming out in the final with respect to this footnote, was that change made for the purpose of concealing anything?

A No.

THE COURT: In that connection -- perhaps I misunderstood you -- I understood you to say that you had nothing to do with these changes as such or, at the very least, you don't recall any discussions with anybody about the change before they became finalized. You see what I am --

THE WITNESS: Yes, your Honor.

THE COURT: Is that a fair statement?

THE WITNESS: That's right. I discussed the

original disclosure.

THE COURT: The original notes, C and E?

THE WITNESS: Right.

THE COURT: But then, looking at the center fold of Government's Exhibit 17B, were all the scratches and interlineations and notes and so on, as I understand your testimony, you had nothing to do with either making these physically or discussing with anybody these changes as shown by these scratchings and interlineations.

THE WITNESS: Not that I can recall.

THE COURT: Yes, not that you can recall. As I understand, however, you do recall, of course, seeing the final changes as they came out in the proxy statement itself as shown over here on the righthand portion of Government's Exhibit 17B?

THE WITNESS: Right, yes, sir.

THE COURT: Mr. Stillman, then I don't understand how he can fairly be asked this question you just asked.

MR. STILLMAN: I think he could be fairly asked, your Honor. He was there at the time.

THE COURT: Wait a minute. You don't see my point, sir. I am not to critize you. I am trying to make a point which may be important here. Be patient with me.

As I understand his testimony, now that I have sought a clarification, he really had nothing to do, that he recalls, with the changes as they were being made and contemplated.

MR. STILLMAN: Yes, your Honor.

THE COURT: The inference I got from your last question is that he did do so and therefore I am puzzled.

MR. STILLMAN: Your Honor, I am taking it in anyway. Whether he did or did not, I am asking the state of his knowledge with respect to the change that was made in this footnote.

THE COURT: Then I thinkwe ought to get a clarification from your own point of view. That is the whole point of my intervention.

MR. STILLMAN: I appreciate that.

THE COURT: I am not trying to badger you. I am trying to get a clarification.

MR. STILLMAN: Judge, I know that, and I appreciate it.

BY MR. STILLMAN:

Q In August of 1969 did anything come to your attention which would lead you to believe that the change that was made was made for the purpose of concealing anything?

A No.

Q You recall the testimony of Mr. Oberlander?

A Yes.

Q You recall that he told us that you asked him to do some work in connection with this proxy statement?

A Yes.

Q I would like you to turn, if you would --

MR. STILLMAN: Just bear with me a moment, your Honor. I lost my slip.

Q We will come to the paper in a minute. Let's use up these next few minutes and get some testimony in.

You recall that Mr. Oberlander did some work at your request?

A Yes.

Q That was in August of 1969?

A Yes, sir.

Q You recall that there came a time when Mr. Oberlander spoke to you with respect to the work that he had done?

A Yes.

Q What is your best recollection of when this occurred and what occurred?

A This was in August of 1969. Mr. Oberlander called me and said that he had some problems with work papers that he wanted to review with Mr. Kurek and Mr. Kurek suggested that I be the one to review it with him, Mr. Kurek was in a bad mood for some reason and he didn't want to talk to Mr. Oberlander.

So I went over to National Student Marketing's office, took Mr. Oberlander's paper and went through the items with Mr. Kurek. We went through it and we sat there and we went through themajor items in that paper.

He indicated to me that a couple of the programs were changed to a fall program or a spring program, he indicated to me that the Syntex contract should be written off.

When we got through with those major items the difference was immaterial. There were some ups and some downs and it wasn't worth the time and effort to even

try to adjust them.

Q Is it a fact, sir, that as a result of your conversation with Mr. Kurek the Syntex contract was written off?

A Yes.

Q You recall, do you not, that the Syntex contract was the largest single item on Mr. Oberlander's schedule? Let me show you Page 2687 of Government Exhibit 13.

A Yes, it is, it is the largest item on that page.

Q In the course of that conversation that you had with Mr. Kurek did youhave any reason to believe that the man waslying to you?

A No, sir.

Q Did you trust him?

A Yes, I did.

Q The fact of the matter is there came a time that you went to work for him, isn't that right?

A That's right.

Q The work that Mr. Oberlander did in August of 1969, was that work that you could have done yourself?

A Yes.

Q In fact, you performed some similar work back in May of 1969, did you not,sir?

A That's right.

Q What was your view of Mr. Oberlander as an accountant in August of 1969?

A I thought he was a tenacious-type of person, he was a young accountant with a little bit of experience, not as much as some of the other people, but he was the type of person that would dig and dig and dig and find the answers.

Q That was the person that you asked to do this review in August of 1969, is that right?

A Yes, sir.

MR. STILLMAN: Would this be a good stopping point, your Honor?

THE COURT: If you would like.

MR. STILLMAN: It is about four minutes of the hour. I would say that I have approximately anotherhalf an hour of examination to complete Mr. Scansaroli.

THE COURT: We will resume -- I have five to 1:00 -- we will resume at ten after. How is that?

MR. STILLMAN:Fine, sir.

THE COURT: Ladies and gentlemen, we will suspend for luncheon. Please come back at ten after 2:00.

MR. MARTIN: May I hand up a memo to the Court, your Honor.

(Luncheon recess.)

(In open court; jury present.)

J O S E P H S C A N S A R O L I resumed.

THE COURT: All right. May we proceed now, Mr. Stillman.

MR. STILLMAN: Yes, your Honor.

DIRECT EXAMINATION (continued)

BY MR. STILLMAN:

Q Mr.Scansaroli, I have opened up Government Exhibit 13 to Page 2654, and the succeeding page which is 2655.

Can you identify those documents?

o This is the SEC review program that Mr. Oberlander used as of May 31, 1969.

Q When you say "as of," you are talking about the review that he did of the May 31, 1969, unaudited financial statements of National Student Marketing, is that right?

A That's right.

Q He dates the work paper August 20, 1969, is that correct?

A That's right.

Q That is the review that we discussed this morning, that is a similar review which was done by you in May of 1969?

A That's right.

Q We also discussed this morning, Mr.Scansaroli, the footnote which appears in the proxy statement in its various forms in evidence, the final of which is Government Exhibit 25, the draft with various notations on it,Government Exhibit 17, and there were some questions put to you with respect to whether or not you had any conversations with anyone concerning that footnote, and your answer was that you don't recall.

Do you remember that?

A Yes.

Q Over the luncheon recess did I call to your attention a portion of your grand jury testimony?

A Yes.

Q You do recall being before the grand jury, do you not?

A Yes.

Q Do you recall being asked this question and giving this answer --

MR. VELIE: I object to this being read to the witness, your Honor, asking him if he has a new recollection of what it is he told us before. He is simply reading in hearsay at this point.

THE COURT: In any event, I quite agree. This isn't an appropriate procedure.

MR. STILLMAN: I am trying to refresh his memory, your Honor.

THE COURT: Let him look at it.

MR. STILLMAN: Of course.

Q I show you Page 58, which has some red markings on it by myself of your testimony before the grand jury on October 21, 1973.

Was that the portion that you read during the luncheon recess?

A Yes, sir.

Q In looking at that, does that refresh your recollection with respect to any conversation that you had with anyone concerning the footnote?

A To a certain degree, yes, sir.

Q All right. Will you tell us how it helps you to recall and what it helps you to recall?

A When we were in the process of preparing this note to these financial statements, we had discussed the fact that it was going to be adjusted retroactively and the fact that there was a need for a note to disclose this matter.

Eventually it was determined to be immaterial, $21,000, so Mr. Natelli and I discussed it throughout this period, and we came to the conclusionthat it didn't have to

be in there. It was just too small of a figure to even worry about. In effect, that is what happened.

Q Do you know whether or not that is a matter which Mr. Natelli spoke to Mr. Otkiss about?

A Yes, it is.

Q I would like to direct your attention to the 14th of August 1969, and that was the date going into the evening, if you remember, that you went to New York to go to the printers.

Do you recall that?

A Yes,sir.

Q What is your recollection of the circumstances which took you from Washington to New York on that occasion?

A I recall that we went up there -- when I say "we," Mr.Natelli and I. I can't recall anyone else with us, but we went up to the printer's office and arrived there between ten o'clock and midnight.

Q What happened?

A We arrivee at the printer's office and the attorneys had already been there for apparently some time. They made the comment to Mr. Randall, who was there or who came with us, to the effect that if the proxy statement was held up, it would be the accountant's fault and not the attorney's fault.

In any event, about --at that time we sent out for something to eat.

After we finished eating, maybe about two o'clock in the morning, one o'clock in the morning some time in that time frame, the material began coming off the presses and it was Mr.Buck's and my duty to foot and cross-foot these statements as they were coming off, to make sure there weren't any errors, to read them for typographical errors, things of that nature.

End 1A

Q Just to go back and look at this document in its final form.

It has, does it not, literally dozens of pages with financial figures in it, is that correct?

A Yes, sir.

Q Were those the things that you and Mr. Buck were reviewing in the course of the evening and the early morning hours of the next day?

A Yes, sir.

Q Were you busy?

A Very busy, yes.

Q How would you characterize the work? Was it tedious?

Was it fun?

A No, it was kind of tedious simply because it was 2, 3, 4 o'clock in themorning and at that point in time if you are not used to being up that time in the morning, you get kind of tired. Doing this type of work, where you are just footing and cross footing figures, it gets tedious, very tedious.

Q Do you have any recollection of the matter of Pontiac being discussed in the course of that evening or the next morning?

A No, sir.

Q When did you leave on the morning of the 15th?

A It was sometime in the morning between 8 and 10 o'clock, I would say.

Q Where did you go?

A I went back to the Peat, Marwick office in Washington and from there I went home, went to sleep.

Q Do you recall in the course of the evening of the 14th or the morning of the 15th, any discussion of the matter of Eastern Airlines?

A No, sir, not that time.

Q Do you recall in the course of that evening or the following morning the arrival of Mr. Dennis Kelly?

A No, sir.

Q Do you have any recollection of any conversation with respect to Eastern Airlines?

A I can only remember one conversation with the Eastern -- with regard to the Eastern Airlines contract.

That was at some time Mr. Natelli and I were in Mr. Natellis office and he was talking to Mr. Otkiss in Philadelphia. He would indicate to Mr. Otkiss that he was required to have the company remove the Pontiac from the proxy statement. At that point in time the company had the Eastern contract which was dated in May but which was not on the books.

Since it wasnot on the books but it was dated in May, Mr. Natelli had a few problems as to whether he should record that contract or not. He discussed this with Mr. Otkiss. They came to the conclusion that they should record the Eastern contract.

Q Do you recall when it was that this conversation took place in reference to the time that you spent in the printer on the 14 or 15th of August?

A It wassometime after that, but I don't know if it was a day or a week after that.

Q Where were you when Mr. Natelli was having this conversation?

A In Mr. Natelli's office.

Q In Washington?

A Yes.

THE COURT: In other words, are you telling us that this conversation you overheard in Natelli's office was after you returned from Pandick Press here in New York?

A Yes, your Honor.

THE COURT: Do you have any idea how long it was, a day, a couple of days later?

THE WITNESS: I think it was within a day or two days after that, within that -- it is hard to say.

THE COURT: All right.

Q Did anything come to your attention during the period that we have been discussing which led you to believe in any way that booking of the Eastern Airlines contract was anything other than a good faith decision?

A No, sir.

Q Did there come a time, and I believe you did tell us this, that you left Peat, Marwick, Mitchell and went to work for National Student Marketing Corporation?

A That's right.

Q When was that?

A I believe it was in October 1969.

Q What caused you to leave Peat, Marwick?

A Several reasons.

For a period of a couple of years I had always been wondering what it would be like to be in private accounting rather than public accounting, and I never made the jump from public accounting into private accounting because I always had something to do, something keeping me going. Something happened at this point in time that gave me the push that I needed to get out of public accounting.

National Student Marketing was convenient, they were right across the street, they needed an accountant and I needed the experience. I went with National Student Marketing.

Q What was it that happened that caused you to make the decision at that time?

A Well, I had more or less set a goal for myself with regards to raises and bonus that come out once a year within the firm and it just didn't hit the goal I had set for myself. So that gave me the push out the door, in effect.

Q Either during the time that you were at Peat, Marwick, towards the end of your stay there, or the time that you were at National Student Marketing, did it come to your attention that Johnny Johnston was doing some work for the August 31, 1969 audit of National Student Marketing's books?

A Yes, sir.

Q Were you aware that he was developing any program with respect to any particular item in the audit program?

A Yes, I was.

Q Was that with reference to the contracts in progress?

A Yes, it was.

MR. STILLMAN: Can I see Exhibit 35, Mr. Velie.

Q Do you recall whether or not you made any suggestions to Mr. Johnston with respect to the work that he was to do on the contracts in progress for the period ending

August 31, 1969?

A Mr. Johnston, after he prepared the program, he asked me to review it and see if I had any suggestions.

Q And did you?

A And I did make one suggestion.

Q I would like to show you Government's Exhibit 35, direct your attention to page 2673. You see there six items at the top which relate to contracts in process.

I direct your attention specifically to item number 7. Is that in your handwriting?

A Yes, sir.

Q What is that entry?

A The entry says "To compare gross profit percentages on completed contracts with the estimated gross profit on uncompleted contracts and account for any major differences."

Q That was a step which you suggested that Mr. Johnston add to the program that he had developed as reflected in Government's Exhibit 35, is that right, sir?

A Yes, sir.

Q With respect to this comfort letter, did you have any participation in the underlying work with respect to the comfort letter?

A I don't believe so, no.

Q During this period of time --

THE COURT: Excuse me, Mr. Stillman.

I am unclear.

When did you go out the door, as you put it, and across the street?

THE WITNESS: I believe it was around the first week in October.

THE COURT: So that you weren't around at any time when the comfort letter was even being discussed, were you?

THE WITNESS: Only at National Student Marketing.

THE COURT: Yes. But insofar as ~~a plea~~ an employee of Peat, Marwick during that period, I take it that there had been nothing done or said so far as you know about the comfort letter?

THE WITNESS: Not prior to October 1st.

THE COURT: All right.

Q During the time that you were working in National Student Marketing Corporation did you become aware that a comfort letter was being prepared in connection with the Interstate Insurance Company transaction?

A Yes.

Q Who, to your knowledge, was working on that matter?

A I believe it was Mr. Johnston and Mr. Cologna.

Q At that same time that Mr. Johnston was working on the comfort letter, do you know whether he was working on anything else for Peat, Marwick?

A He was making or working on the audit for the year ended 8-31-69.

Q Do you recall his testimony here that he was actually working in your office over at National Student Marketing Corporation? Do you recall that?

A Yes.

Q During the time that he was doing this work and looking at these contracts in progress and everything else that he was doing were you in any way concerned about the work that Mr. Johnston was doing?

A No, sir.

Q Did you feel that there was anything that Mr. Johnston would work on that in any way reflected adversely on yourself?

A No, sir.

Q You recall at the end of the Government's case Mr. Velie read in a portion of your testimony at the Securities and Exchange Commission. You recall that?

A Yes, I do.

Q How long did you remain with National Student Marketing Corporation?

A Till May 1st of 1970.

THE COURT: 1970?

THE WITNESS: Yes, your Honor.

Q Two things happened on that day, is that right?

A Yes.

Q What are the two things?

A National Student Marketing moved to Chicago and I got married.

Q What was the reason you left National Student Marketing Corporation?

A Well, I had just gotten married and I did not want to relocate to Chicago.

Q After you left National Student Marketing, did there come a time when you were told or learned that the Securities and Exchange Commission wanted to talk to you?

A Yes.

Q How did you learn of that?

A I don't recall if I received a phone call or if I received a letter. I don't remember.

Q Regardless of which way it was that you learned of it, did you go down to the SEC?

MR. VELIE: Your Honor, I think we are getting well beyond the scope of any of the case here and into what may be simply self-serving hearsay, prior consistent statements

by a defendant.

THE COURT: I don't know about that at all, but I see nothing wrong, since we already know that he was asked questions by the SEC, and that has been brought out by you and Mr. Stillman on a number of occasions, I see no harm in this, even though it is a bit repetitious.

MR. STILLMAN: Thank you, your Honor. It will be short. There will be two or three questions.

Q When you went down to the SEC to answer their questions, did you have an attorney?

A No.

Q Was there any reason you didn't have an attorney?

A I didn't think I needed one.

Q The portion of your SEC testimony which Mr. Velie read dealt with the tax matter that you had previously discussed with Carol Raimondo and the tax matter that becomes a part of the entrywith respect to the Michaels retroactive adjustment, is that correct, sir?

A Yes.

Q In that testimony I believe you indicated that it was decided, or learned, that the error which Miss Raimondo had brought to your attention was in fact itself an error. Do you recall that?

A Yes.

Q Who was the person who made that subsequent discovery?

A I did.

Q How did it come about that you made that discovery?

MR. VELIE: Your Honor, I believe we have really gotten well beyond --

MR. STILLMAN: I couldn't disagree more, your Honor.

THE COURT: I am sure you couldn't, but that is not really the point. This is an objection which I am going to sustain in part because I don't think it is necessary that we go into all thehow did he come to until at least we find out from him when this was.

MR. STILLMAN: All right, sir.

Q When was this, sir?

A I believe it was during the early part of 1970. Mr. Ford of the Securities and Exchange Commission had called me and I believe we had several telephone conversations and he was trying to determine the computations and the errors that were made in the deferred tax liability and subsequent to that I believe a letter was sent out by somebody at the SEC asking for some type of explanation.

At that point in time I was with National Student

Marketing Corporation and I was given the question to answer.

Going through all the documents I had, the tax return, I came to the conclusion that the taxes in the proxy statement were incorrect, and what I did -- I believe this was on a Saturday -- I left a note with Mr. Kurek, and I put a copy of the note on Mr. Natelli's desk, indicating that I thought an error had been made, so that he could check it out to make sure or his Tax Department could check it out.

Q To the best of your knowledge, was that information conveyed to the Securities and Exchange Commission?

A I believe it was, yes, sir.

Q Mr.Scansaroli, in the period from August of 1968 until the time that you left National Student Marketing or, indeed, until today have you ever been concerned that as a result of anything that you did in connection with this audit you would lose your license to be a certified public accountant?

A No, sir.

Q To the best of your recollection, sir, and on your oath, do you recall ever expressing to anyone any concern that you would lose your license with respect to anything that you did on the National Student Marketing Company audit?

A No, sir.

Q Have you ever, sir, prior to this lawsuit, been the subject of any disciplinary proceeding by the Securities and Exchange Commission?

A No, sir.

Q Have you ever been subject to any disciplinary proceeding or any proceeding which attacked your professional standing before any licensing authority?

A No,sir.

Q Prior to the time that you came to court in this case had youever been in a courtroom before in your life?

A No, sir.

Q Mr. Scansaroli, did you knowingly or intentionally do anything in connectionwith the preparation of this proxy statement which you knew to be false or misleading?

A No, sir.

Q Did you do anything at all in connection with the work that you did as an accountant, as an auditor, in the affairs of National Student Marketing Corporation which represented anything other than your good faith best efforts to do a job for your client?

A No, sir.

Q So help you God?

A So help me.

MR. STILLMAN: I have nothing further, your Honor.

THE COURT: Mr. Martin.

MR. MARTIN: Nothing, your Honor.

THE COURT: Mr.Velie.

MR. VELIE: Yes, your Honor.

CROSS-EXAMINATION

BY MR. VELIE:

Q Mr.Scansaroli, this morning do you recall explaining to this jury that generally audit work would be done anywhere from a month to three months to six months after the client's year end?

A Yes.

Q Do you recall explaining to Mr. Stillman the reasons as follows:

"We have to wait until the books are closed. The client can make whatever adjustments they think should be made. Many times it takes weeks after the year end before the company can close its books."

You gave that answer this morning, didn't you?

A Yes.

Q You gave that answer under oath?

A Yes.

Q That answer is not exactly the truth, is it, Mr. Scansaroli?

A I think it is, yes.

Q I am going to show you Government Exhibit 4C in evidence,which is your general binder, is that right, for the audit?

A Yes.

Q I am going to read to you from Page 1500, which is the commercial audit program guide introduction, Paragraph 2 on Page 1500.

"In considering the time at which auditing procedures should be carried out emphasis should be placed on adequate time for planning engagements so that a sub-

stantial portion of our examination is carried out prior to the year end."

A That's right, but if you are going to do interim work, right. We didn't start this audit, we weren't -- we were not retained as the auditors until the end of August, which was the end of their fiscal year. There was no way in the world we could start that audit prior to that. You know that. Why do you give me that kind of a question?

Q Mr.Scansaroli, then the reason you didn't do it was you weren't retained?

A That's right.

Q It wasn't because the company hadn't closed its books?

A But the normal procedure is you cannot make an audit until three, four, five weeks after the company's year end. That is just a normal procedure.

Q That is not reflected in your audit manual or in that particular binder, is it?

A I don't understand the question.

Q In any event, you began the work in late August, is that correct, Mr.Scansaroli?

A Yes, sir.

Q At that time you were the most experienced supervisor at Peat, Marwick & Mitchell's Washington

office, is that correct?

A I would think so, yes, sir.

Q Some time after you began that audit trial balances were prepared, is that correct?

A Yes,sir.

Q The first trial balance, you don't dispute that that shows a loss for the company, do you?

A No, I don't dispute that.

Q We have seen it here in evidence. It is dated September 25. There was a loss for the company according to that trial balance, is that correct?

A Yes.

Q You never even heard of unbilled accounts receivables, fixed fee contracts in progress, until halfway through that audit, is that correct?

A On this audit?

Q Yes, sir.

A That's correct.

Q The second or third week of October?

A In that area, yes, sir.

Q At that time your testimony is that Mr. Randall and Kurek said that this is how they want to do it and how they have been doing it, is that correct?

A Yes.

Q You told us this morning how you went down to Arthur Andersen's office, the predecessor accounting firm, is that correct?

A Yes.

Q You never spoke to Arthur Andersen's accountants about unbilled accounts receivable accounting, did you?

A No.

Q You never checked to see if they wrote a management letter which mentioned this particular thing that the company had been doing for some time, is that correct?

A That's correct.

Q You know what a management letter is, don't you?

A Yes, I do.

Q It helps the company do its work, is that the idea?

A I imagine the letter is a letter to the management of the company telling them the weaknesses that have -- that the auditors may have noticed in current control or accounting procedures and their recommendations to correct those weaknesses.

Q You have written management letters, is that correct?

A Yes, I have.

Q They are a useful place to look to see what the weaknesses might be in the company's internal control procedures, is that correct?

A I would say yes.

Q Internal control is a matter of extreme importance in an audit, is it not?

A I wouldn't say extreme importance, no, sir.

Q You would have to concede, wouldn't you, that if internal controls are weak the auditor must extend his procedures to make sure that what is said on the financial statements is so?

A Generally speaking, that's right.

Q In fact, you prepare or you have to prepare for each audit a lengthy internal control questionnaire, is that correct?

A That's right.

Q One of the first things you are supposed to do in an audit, is that right?

A Yes,sir.

Q In any event, you didn't look at the management letter?

A I can't recall, no, sir.

Q You didn't even look at the company's interim

financial statements, did you?

A I can't recall.

Q You can't recall?

A I may have. We may have had a copy of that in the permanent file, but I am not sure.

Q First of all, just so we all know what we are talking about here, I am going to show you what has been marked as Government Exhibit 46, I believe it is, A. While it has a Government exhibit number, Mr.Scansaroli, I believe you and the jury will all recall that was marked by Mr. Stillman in his examination of Mr. Kurek, Government Exhibit 46A in evidence offered by your lawyer.

nd 2B

MR. STILLMAN: Is that a question or a speech?

Q That is what it is, isn't it?

A This is a financial statement for the nine months ending '67, '68.

Q That is one of the so-called interim financial statements, is it?

A That's right.

Q Okay. Which is your answer with respect to whether you had examined interim financial statements or any underlying work papers, that you didn't or you don't recall?

MR. STILLMAN: I think there are two questions, your Honor, interim financials and underlying work papers.

Q Did you ever examine any underlying work papers for the interim financial statements?

A No, I hadn't.

Q You weren't asked in seeing how contracts in progress were handled previously?

A You mean on quarterly statements?

Q Yes.

A No.

Q You weren't interested in that?

A It never dawned on me that I should look at it.

Q Do you recall telling the grand jury that you

didn't recall seeing any interim financial statements?

A I don't recall.

MR. STILLMAN: Page, Mr.Velie?

MR. VELIE: 19.

Q I will do it this way. You do recall testifying in the grand jury?

A Yes, sir.

Q That was on October 31, 1973?

A I would say yes.

Q You were under oath to tell the truth that day?

A Yes,sir.

Q "Q Did you see during the course of your audit any financial statements that had been prepared by National Student Marketing Corporation during the course of the last 12 months?

"A I don't recall seeing any."

Do you recall that question and answer?

A I don't recall it, but I will take your word for it, it is in that book.

Q You never checked the method that they had been using during that preceding year for recording contracts in progress, did you?

A You mean during the current year?

Q During the year which you were auditing, you never checked the method?

A No, I didn't.

Q Just so there is no question about it, all of your work with respect to the unbilled accounts receivables then was done some time after you first learned of it, which I believe you told us was the first or second week of October, is that correct?

A Yes, sir.

Q In fact, the method of booking unbilled accounts receivable which you and Mr.Natelli approved for National Student Marketing was a complete departure from the preceding year, wasn't it?

A I am not sure. I don't know.

Q Did --

A Excuse me, I am sorry. I believe that the previous year they did have some contracts, but I don't know how many. I know it wasn't a material amount, but they did record contracts, I believe.

Q How did you know that if you didn't check any of the things I just asked you? Were you assuming that?

A I know that now.

Q You know that now?

A Yes.

Q What did you know then? You have told us that you didn't check the system that you had been using during the preceding year, you didn't look at the interim financials, you didn't look at any work papers underlying the interim financials and you didn't talk to Arthur Andersen or read their management letter, right?

A Right.

Q We have it.

MR. STILLMAN: Excuse me. I do object to -- he can ask all the questions he wants to ask. It is a rehash of five questions. I object to the form that he is proceeding in.

THE COURT: Overruled.

Q So that back there at the time, I take it you didn't know if you were changing something or not changing something, is that correct?

A If I was just changing the method or not changing the method of accounting?

Q Yes,sir.

A I would say no, I did not know at the time.

Q In fact, it was after all an important change, wasn't it?

A I don't think it was an important change, no, sir.

Q You don't think it was an important change. You

just told Judge Tyler this morning in response to his question, "Yes, sir, if you call that a change, I'm not so sure it is a change."

A Judge Tyler is asking me the difference between what the client was doing during the year and what we did at the end of the year. He did not ask me what the difference was between the previous year and this year. It was during the same year. The client was recording the contracts. The only thing is, they were recording the whole contract and we suggested they record a percentage of that contract. It was in the same year.

Q You heard Mrs.Raimondo testify yesterday. Do you have Exhibit 3 up there?

Do you recall Mrs. Raimondo's testimony?

A Yes, sir.

Q Do you recall that she said that the method previously of recognizing income was to accrue income according to contract terms, signed contracts and she underlined the signed.

A I recall that.

Q In fact, at year end you and Mr. Natelli okayed a procedure in which they simply told you about oral commitments to sign contracts in the future, is that correct? And that is the point in time in which you took down income

And recognized it?

A We recognized income at the point that the client made the oral commitment, yes.

End 3A

Q That's a change, isn't it?

A From the previous year? Well, based on what I know now, I would say it was not a change simply because the amount was immaterial last year. If it is immaterial, I don't believe you can call it an accounting change as such.

Q Let me see if I understand your answer. You say in the preceding year the number of contracts in progress or the amount of them was so small that now if you do it on an oral basis instead of a contract basis there's no change?

A It is not a change from a contract or an oral basis. It is a change from a completed contract to a percentage of completion basis.

Q Now you are saying that they didn't have percentage of completion prior to your implementing it, is that the idea?

A That's right, yes.

Q All right.

Another change Mrs. Raimondo noted was that costs associated with the contracts previously were costs which had been incurred, is that correct?

A Yes.

Q Incidentally, you agreed with this analysis of Mrs. Raimondo's, didn't you? She so noted it on the memo-

randum?

A Yes.

Q Do you have my preceding question or would you like it read back.

A Please read it back.

Q The second change Mrs. Raimondo was talking about was the fact that before you and Mr. Natelli made the changes, the company used to record the costs associated with the contracts it had as they were incurred.

A That's what she said, yes, sir.

Q The change that you and Mr. Natelli put in was that these costs would be accrued, is that correct?

A First of all, I'm not so sure Mr. Natelli and I put this change in that you keep saying. The company as I was saying was recording these contracts for the first three quarters. The only difference was they were recording it, the whole contract, you have to record a percentage of that contract. It was not a change in accounting method, it was just a change in the amount of the contracts as we recorded. It was still percentage of completion basis in effect except they recorded the whole thing, if that's possible.

Q So it is percentage of completion? I thought you said the opposite before.

A See, what happened is the client recorded the

contract in the same manner as it was recorded as August 31, 1968. The only difference was that during the first three quarters they recorded the whole contract. We said you should record a percentage of that contract.

Q That's the only difference.

A From the first three quarters to the year end, yes, sir.

THE COURT: Wouldn't you agree that that's a major point of distinction between a percentage of completion and completion of contract accounting system?

THE WITNESS: No, sir, I don't think that -- I don't believe that it is a change in method. Let me give you an example that might help. If Ford Motor Company came to me and says I have got a commitment with National Student Marketing for $10,000, National Student Marketing would record $10,000. The way we set it up, 90 per cent complete, we only record $9,000.

It is recognizing income, and at the same point in time, the difference is how much of that do you recognize.

THE COURT: Again, isn't that typical of a percentage of completion method?

THE WITNESS: The only two things, you have to complete a contract method and percentage of completion method. A contract method, everything has been completed.

Let's take, for example, putting up an office building. Income is not recognized on a completed contract basis until that building is fully completed and the bill sent out. On percentage of completion basis the income is recognized as that building is progressing.

THE COURT: Right. In effect, my question to you can then be put. Isn't that what you and Natelli suggested to NSMC in the fall of 1968, and that it was different so far as you know from what had been going on theretofore?

A It was -- I would say it was different, yes, sir, from the three quarters to what was done at year end. It was different.

THE COURT: All right.

Q It was the other difference you already told us about in that now the income gets recognized when the salesman says he has a commitment from the client of an oral nature, is that correct?

A I just said that was not a difference. They were handling or recording the income for the first three quarters at the same point in time.

Q You knew that without checking their interim financials, the work papers or talking to Arthur Andersen or reading the management letter?

A That's what they told me.

Q They told you that?

A Mr. Kurek and Mr. Randall told me that, yes, sir.

Q Let me see if I understand you basically.

Do you say that this is an important change or not?

MR. STILLMAN: Which is the change now?

MR. VELIE: Whatever change he says it is.

Q Was it important in your view or not?

A If there was --

MR. STILLMAN: I --

THE COURT: You object?

MR. STILLMAN: He seems to be ready to answer, your Honor. I have trouble understanding where he is at.

THE WITNESS: I'm not sure I understand the question either.

THE COURT: It is only fair you understand that. I think you better rephrase it. I think Stillman's instincts were better thanwhat he said.

Q Tell me, Mr. Scansaroli, you have described certain differences, is that correct?

A Between what and what?

Q Between the way the company had been doing its contracts accounting prior to the change made by you and Mr. Natelli after year end and the changes which were in fact

made?

A There was one change between the first three quarters of the year and what was done at the end of the year.

That change was changing from the -- recording the whole contract to recording a portion of that contract.

Q You say that wasn't much of a change?

A Yes, I would say that was a significant change.

Q I thought you told Judge Tyler this morning it wasn't much of a change?

MR. STILLMAN: It is argumentative, your Honor.

THE COURT: I will sustain that.

Q Do you recall your testimony this morning in which you said that it wasn't much of a change?

A I recall testimony something to that effect, yes, sir.

Q Which is it?

A You are asking me questions in different veins. Now, the change as far as I am concerned from recording the entire contract and the percentage of completion at a given point in time -- recording both at the same point in time is not a major accounting change. It is a major change in the amount that you record, but in an accounting sense I don't think you can say that's a major change.

Q Would you say that it is fair to say that in the year ended August 31, 1968 was the first time that NSMC attempted to record contracts under a new and unique accounting procedure?

A They were recording contracts under the method we just described during the first three quarters of this year.

Q Was it new and unique or was it not?

A You know, you can describe things in a million and one different ways. Sometimes you could say it was unique, sometimes no. It depends on how you are phrasing this and who you are talking to.

Q You talk to this jury, sir, please, and tell them

was this a new and unique system of accounting or was it no change whatever?

MR. MARTIN: I am going to object to Mr. Velie --

THE COURT: Sustained to this extent, Mr. Velie. This question is susceptible, it seems to me, of a number of interpretations. You mean new and unique unto NSMC --

MR. VELIE: Yes, sir.

THE COURT: -- new and unique generally to the field of accountants in this wide nation? It could be anything. Which is it?

Q Let's take the new and unique to NSMC.

A For 1968, for the entire year, yes, sir.

Q Your answer is that it was new and unique?

A For NSMC, yes.

THE COURT: Would you brook an interruption here for the afternoon recess, Mr. Velie?

MR. VELIE: Yes, your Honor.

THE COURT: Very good.

Ladies and gentlemen, the recess.

(Recess.)

BY MR. VELIE:

Q Mr. Scansaroli, do you recall this portion of Government's Exhibit 4C in evidence at page 1469 and page 1470

A Those are review notes.

Q Is that what you call a points sheet? Do I have that right?

A I am not sure I ever heard of a points sheet. Those are what we consider to be review notes.

Q Aren't these things to do before completion of the audit?

A Not necessarily. It depends on the note. These are notes that are made when somebody reviews the work papers. Some may be comments, some may be things to do, thing of that nature.

Q It says right at the top, doesn't it, "National Student Marketing Corporation, to do before completion of audit 8-31-68."

A Yes, sir.

Q Do you recall that one of the things Mr. Natelli asked you to do in writing is this, at page 1470. "Establis a case from the facts as to why we should have the contracts booked as of August 31, 1968."

A That's the reason for the memo in our special sales binder.

Q Exactly, and that is the one Mr. Stillman was reading from this morning, from which Mr. Martin and I have had occasion to read previously, is that correct?

A That's right.

Q Exhibit 3, your special sales work binder.

In this it is fair to say, isn't it, that you canvas or go over analytically possible ways of booking income on the contracts, is that correct?

A That's what the memo says, yes, sir.

Q The first one that you talk about is recognize income the date the work is performed.

A Yes, sir.

Q What did you understand National Student Marketing's work to be, what was it they were doing for clients.

A It depended on the program. One program was to put posters on campuses, one program was a mailing of a collage that they would send out to college and high school students.

Q You rejected the notion that they should recognize income after they had done their work, putting up ch posters and mailing out the mail, is that the idea?

A That work was done by third parties.

Q In any event, you thought that that was not a good time to recognize the earnings?

A That's right.

Q You thought that it should be recognized earlier, is that correct?

A That's right.

Q In fact, you thought a good time to recognize it would be when the salesman said he had a commitment from the client to sign a contract later?

A When a client said that he had a commitment.

Q He would say that to the salesman, wouldn't he?

A He would say it to the salesman, yes, sir.

Q Correct me if I am wrong. I take it that what you were trying to get at here is in some way to match the revenue that would one day be earned when they had done the work and were paid with some costs that were associated with earning that revenue, is that the idea?

A I don't think that is right, no, sir. We were trying to match costs with revenues.

Q I thought I said that, but you correct me if I

am wrong. You were trying to match costs with revenue, right?

A Yes, sir.

Q The revenue would be in fact received some time after they had done their work or while they were doing their work? Do I have that right?

A I don't believe that is a proper description of revenue. Revenue does not necessarily mean that you have to receive it, unless you are on a cash basis or something like that.

Q Let's put it --

A Revenue are the sales when recognized. That is the revenue of the company.

Q And you are trying to find the right spot to put that, so you are going to put that where the costs are, is that the idea, when the costs in fact take place?

A Yes, we are trying to match costs with revenues.

Q The costs that you associated with these particular contracts were accrued costs, weren't they?

A No, sir.

Q They weren't accrued costs?

A No,sir.

Q Were they incurred costs?

A Yes,sir.

Q You had entries showing what National Student Marketing actually owed to people for these contracts?

A We were trying to match costs with revenues. We were trying to match overhead costs with revenues.

The direct cost was recorded at the same time the revenue was recorded. There was no problem there. That cost was matched with that revenue. We were trying to match overhead costs with revenue.

Q What overhead costs were you talking about?

A Talking about salesmen's travel expenses, talking about secretaries' salaries, talking about rent, depreciation, interest, utilities, telephone, those type of costs.

Q You estimated those costs, is that the idea?

A No, sir. They were actual costs.

Q Did you know which one went with which contract?

A No,sir. That was the problem we faced. We could not --

Q So you had to estimate some for each contract, is that the idea?

A We did not do that, no, sir. That is why we did not do that, because it was almost impossible to do something like that. You could not tell what rent, for example, went to any individual contract.

Q One of the costs that you thought ought to be

matched is the salesmen's commission, is that correct?

A I am not sure I did. I would have to look at the work papers and see which costs had to be matched with revenues.

Q Were not the salesmen's commissions a part of the accrued costs and liabilities on contracts in progress?

A Yes, they were.

Q Those are some of the costs you were trying to match with the revenue then?

A Well, those were direct costs. They were recorded automatically when the revenue was recorded. Like I said, there is no problem recording the direct cost. The problem was the indirect cost.

Q Let me just ask you this: You knew that the salesmen weren't even entitled to their commissions yet on these oral commitments, didn't you?

A They were not entitled to the commissions?

Q That's right.

A Yes. That's right. They were not entitled to commission until the third party completed their portion of the work.

End 4B

Q In fact, you knew that the salesmen hadn't even really nailed down the business orders yet from which this revenue would some day be earned, is that true?

A I am not sure I understood what you mean by business orders.

Q These salesmen hadn't even really secured the business from which the revenue would be earned?

MR. STILLMAN: I don't understand the question.

A We think that the income -- the revenue was secured, yes, sir.

Q You did think that the revenue was secured?

A Yes, sir.

Q That the salesmen had these orders and they were real good, tight orders, is that right?

A I am saying that we said that the income was earned at the time the client company said that they had a commitment with NSMC.

At that point in time the income was earned.

Q I am asking you a slightly different question The question I am asking you is: These salesmen weren't even sure that National Student Marketing would have the business from which these contracts were supposed to produce income?

A That is not true. As far as I was concerned,

the salesmen were sure. That is the only reason we recorded it. We would not have recorded those contracts if the salesmen were not sure.

Q Then it is an important point, isn't it? If the salesmen weren't sure, you should not have reported the income, that is fair to say, isn't it?

A Yes, sir.

Q All right. This morning you testified in response to some of Mr.Stillman's questions, Page 1499. He was asking:

"Q Do you recall whether Mr. Randall gave any reason as to why he would prefer that you not confirm in writing?"

Do you recall that question?

A Yes, sir.

Q Your answer, sir, "He gave two reasons. One, he indicated that the people in the advertising field were kind of fidgety people and didn't want to be bothered by auditors, and, secondly, the way in which corporations sign contracts is that the process of getting a contract within a corporation is chain of command until it comes to a legal department is a long, tedious process. He didn't want us to confirm them in writing because some of the people involved are not aware yet that this has gone through the chain of command yet, and, therefore, he would prefer we

find some other way to satisfy ourselves."

Do you recall giving that answer?

A Yes,sir.

Q You alreadytold us when you testify in the grand jury you were under oath.

A Yes,sir.

MR. STILLMAN: We have established that.

Q Do you recall giving this answer --

MR. STILLMAN: Page?

MR. VELIE: 42.

Q "Do you remember who it was specifically that gave that request?"

MR. STILLMAN: What line?

MR. VELIE: Line 14.

Q "A It would be Cortes Randall.

"Q Did he give a reason?

"A The reason for not confirming them in writing was that it was a special type of situation, where the salesmen were dealing with these various clients and they were at the point that they thought that if they pushed the clients too hard, that they would stick them in the back some place or they may say we are busy, we don't have time to sign the contract. They felt it was a touch and go situation between the account executive and the people he was dealing

with. In many cases it was also with the ad agency. They didn't want to push the ad agency because the ad agency in this case had some power as to who would do the advertising."

You gave that answer, didn't you?

A I am sure I did. If that is what you are reading from my testimony, yes, sir, that is what I recall at that point in time. I had not looked at any work papers, I had not refreshed my memory on any of this for several years. Now that I have looked through the work papers, I am giving you the answer now that I can best recall.

Q So your testimony, just so I understand it, is while you told that to the grand jury under oath, you didn't really remember it then, but you remember it better today?

A That's what I remembered at that point in time, yes, sir.

Q Today you remember it better.

A Yes, sir.

Q So that what you told them, that's not true?

A At this point in time? At that point in time it was true. I was under oath. I had to tell to the best that I could recall.

Q All right. I believe this has been read to you already today.

MR. STILLMAN: What exhibit is that?

MR. VELIE: Exhibit 3, page 1912.

Q "Under this method," and I think we will all agree this is the method you ultimately adopted, "extra caution should be used because there is no legal binding contract. The proper files must be maintained on both the company and the account executive in addition to statistical data on all clients."

Let's take this part about extra caution first. Did you use extra caution in your audit?

A The extra caution that I was talking about was

that the company had to maintain proper records. I think if you read the rest of that sentence, it indicates that we were talking about the company's records. They had to use extra caution, use extra diligence to make sure that they got the proper documentation from the account executives.

Q The company did not keep proper records, did it?

A They weren't like they should be, no, sir.

Q It is fair to say, isn't it, that "accounting bookkeeping and maintainance of files were almost forgotten"?

MR. STILLMAN: Are you reading from something?

MR. VELIE: I'm reading from Mr. Scansaroli's handwriting on page 1970 of Exhibit 3.

A That's right, yes, sir.

Q "This was especially true in the area of contracts, account executives and other files and data with regard to gross income on contracts."

So it is especially true that they didn't have good contract files or account executive files, is that correct?

A Yes, sir.

Q "Thenet result is that our working papers represent the beginning of proper record keeping and accounting procedures for reporting gross income on contracts."

Is that true, too?

A Yes, sir.

MR. STILLMAN: That was reading again? Was that something you were reading, Mr. Velie?

MR. VELIE: Yes, it was.

MR. STILLMAN: Okay.

Q Do you recall Judge Tyler asking you some questions this morning with respect to maintenance of records? I'm going to read from page 1506.

On the other hand, would it not be fair to say from your professional viewpoint that in order for percentage of completion method of accounting to work that presupposes complete and accurate records of work in progress and accounting or financial records relating to each one of the contracts or deals?"

Your answer, "Yes, sir."

"The Court: And absent those data the percentage of completion method becomes somewhat chancy and ineffective from an accounting point of view?"

Your Answer, "Yes, sir."

Just to put a point on it, the accounting method that you and Mr. Natelli landed on then was somewhat chancy and ineffective to say the least, wasn't it?

A That's Judge Tyler's terminology.

Q You answered "Yes, sir."

A I'm thinking in different terms, although I agree he said that. I agree to his terminology.

Q I thought you agreed that was a fair statement?

A It is a fair statement, yes.

Q His statement was a fair statement?

A Yes, sir.

Q You don't disagree with it?

A No, sir.

Q Mr. Scansaroli, you told us that the reason your answer to the grand jurors was not an accurate answer was that your memory is better today than it was in the grand jury, is that correct?

A Because I reviewed all the documents, yes, sir.

Q Was your memory still in a primative stage on March 22, 1971? That was a little bit closer to the fact, wasn't it?

MR. STILLMAN: I object to the form of the question.

Q Let me ask you, what was the state of your memory in March of 1971?

A I had not looked at any documents as of that date.

Q Do you recall this question and this answer when you testified under oath before the SEC, page 61, line 12?

"Q Did you know in this circumstance whether you couldn't get written confirmations from these clients?

"A No, I am not saying we couldn't, I am not saying that, I am not saying the client's wouldn't confirm. What I am saying is that we got to a point where we did not want to upset anybody or irritate anybody and ~~would~~ they'd say forget about it. In this type of business it is touch and go and therefore we decided we would not confirm them on a written

basis."

You go on to say you would do them by telephone.

A That's basically what I said in the grand jury testimony, is that correct?

Q That's correct, and you said the three years before that too, in the SEC, is that correct?

A That's what I recalled at the time.

Q Twice you said it was touch and go.

A That's what I recalled at the time.

Q Today you say it is not touch and go.

A I would say that I have had a lot more chance to review all the documents and I have a better picture of what happened.

Q Let me just ask you, did you use extra caution in confirming these receivables?

A I think we did everything we could possibly do, yes, sir.

Q Everything you could possibly do. All right.

Let me just ask you, you testified on your direct examination about the importance of independence as a CPA, is that correct?

A Yes.

Q That is important, isn't it?

A Yes, sir.

Q I think you also told us one of the reasons you left Peat, Marwick, Mitchell and Company was that you had set yourself certain goals as to promotions and pay increases, is that correct?

A Yes, sir.

Q During the 1968 audit National Student Marketing Corporation offered you a job, isn't that correct?

A During the 1968 audit?

Q Yes, sir.

A I don't believe so.

Q You don't believe so? I am going to just read you a little bit of your grand jury testimony, page 8, right at the very bottom.

"Q Why was it that you left Peat Marwick and Mitchell to become an employee of National Student Marketing Corporation?

"A I left St. Francis College and went directly into public accounting. From that time up until I left Peat, Marwick, I was in public accounting. I was also wondering what it would be like to be in private accounting. It is a little bit different. In public accounting you go in and audit the books. In private accounting you work up the figures and put them in the books. This was all in the back of my mind. So in 1969 I had set a goal for myself with Peat,

Marwick and made up my mind that I wanted a raise to a certain amount of money and I wanted certain promotions and if they didn't meet those goals I was going to leave -- it was close, but it wasn't what I expected, so it gave me a little push to leave public accounting and go into private accounting. That's the reason I left.

Q Did National Student Marketing Corporation make you an offer that seemed desirable to you?

"A Yes. They made me an offer prior to this. Most clients when you audit them, if they need accountants, they will approach you and ask you to come to work for them. Since I didn't know where I was going to go, this seemed like the best place to go, I was right across the street, I told Bernie Kurek at the time that if he still wanted me I would like to come over there and work for him and he said yes."

It was prior to that that you got the offer, wasn't it?

A They made me an offer -- they made me an offer several times during 1969, but I don't think it was during the audit of 1968.

Q So that when you say "most clients when you audit them, if they need accountants, will approach you," that was just a figure of speech?

A This is a general term. What I am saying is that most accountants will get offers from their clients if they need accountants.

Q Your testimony was you didn't get your offer the way sometimes happens when you are auditing, but later, is that your testimony?

A I am saying I talked to these people for about ten, twelve months and several times they made me an offer to go to work for them as an accountant, but I am saying I don't believe it was as of the audit for '68, I believe it was subsequent to that. I could be wrong, but that's my recollection.

Q You kept that offer in mind, in any event, is that right?

A Well, I never thought about it until I was ready to leave. Then I kept it in mind, I thought about it at that point.

Q Let's just see about this extra caution, doing everything you could.

MR. STILLMAN: Move to strike.

THE COURT: Yes, we will strike and disregard.

Q Let me just see if I have it right. I believe you told us that you did everything you could to audit these contracts in progress. Is that your testimony?

A I am sure I said that, yes.

Q You didn't keep control of the confirmation process, did you?

A In some cases the account exec made the telephone call for me.

Q You recall when Mr. Johnston was on the stand he told us how he performed the confirmations in 1969, written confirmations? You remember that?

A Yes, sir.

Q He or whoever was working under him actually kept in their own hands the envelopes and the confirmations addressed to the clients, is that correct?

A That's right.

Q Not Peat Marwick's client, National Student Marketing, either, people who owed National Student Marketing the money, is that right?

A That's right.

Q He kept control of those mailings so nobody could touch them but the auditors?

A That's what we normally do when we send out written confirmations.

Q That's a better procedure, isn't it?

A Yes, you have better control than you do usually when you make a telephone call.

Q So you would have to qualify, wouldn't you, your answer that you did everything you could? You could have kept direct control, couldn't you have?

A Not -- let me think about that a second. We could if I would have made all the telephone calls directly. I guess I would have to agree with that question, yes.

Q So you didn't do everything you could with respect to keeping direct control?

MR. STILLMAN: Repetitous.

MR. VELIE: I am just going for a point here.

A In that respect, I have to agree, in that respect, yes.

Q Incidentally, in addition, you didn't always speak to the client himself, that is, you didn't speak to the debtor of National Student Marketing to find out if in fact the money was owed or was forthcoming, did you?

A We confirmed with different types of people in this respect, sometimes with company personnel, sometimes with the ad agency who in effect was doing the advertising for their client. In one case I found out that I also talked to I. S. Berlin, who was a printer who was on NSMC's records, the contracting officer.

Q We will get to that. Would you agree, sir, that it is a better audit procedure to make a contact directly with the debtor and not with some agent or intermediary?

A I would say in most cases, I would say that is probably true.

Q So there is a second qualification to your statement that you did everything you could, is that correct?

A If you want to pull these fine points out, yes, sir.

Q Fine points?

A I think they are fine points that you are pulling out, yes.

Q I see. I believe on your direct examination you told us that you thought at the time you contacted Frank Salgan of I.S.Berlin that he was a representative of an advertising agency, is that correct?

A That's right.

Q What made you think that?

A He was the contracting officer and I was either talking to the ad agencies or the clients themselves and that is the contracting officer on the forms that we were using.

Q How did you know who in the world you were

talking to on the telephone? Did you dial a number that you found in a directory in place?

A The numbers were furnished to me by personnel at NSMC.

Q And you just dialed the numbers that were given to you?

A That's right.

Q What did the person who answered the telephone say? Did they say that this was an ad agency?

A In some cases, yes.

Q I am talking about I.S.Berlin. Did they say, "I.S.Berlin Press"?

A I don't recall.

Q Are you quite sure that you didn't have a clue that I.S.Berlin was in fact a printer for National Student Marketing back there when you did your audit?

A I don't think I did, no, sir.

Q You are pretty sure?

A As far as I know, I didn't know that.

Q Let's see if we can give you some help. Government Exhibit 4B, a portion of which is in evidence, is the National Student Marketing Corporation liabilities and expense binder relating to the August 31, 1968 audit, isn't it?

A Yes, it is.

Q You were the supervisor on that audit, is that correct?

A That's right.

Q You supervised Mr. Oberlander's work in part?

A Yes,sir.

Q At times you made checkmarks on Mr. Oberlander's work?

A Yes,sir.

Q That is after you reviewed the piece of paper that Mr. Oberlander had been working on, is that correct? You didn't just put checkmarks down, you must have reviewed something?

A That's right, yes, sir.

Q You reviewed carefully?

A I would think so, yes, sir.

Q You would read the page?

A I would read the page.

Q Tell me, Mr.Scansaroli, on October 18, 1968, did you initial and date this page?

A Yes, I did.

MR. VELIE: Page 1725, gentlemen.

Q The third entry on this page is for I.S.Berlin Press, isn't it?

A Yes, it is.

Q This is accounts payable by National Student Marketing, that is, money NationalStudent Marketing owes to various people who sell them things?

A Yes,sir.

Q Entry Number 1 is for the Columbia Printing Company, is that correct?

A Yes.

Q Entry Number 2 is for the City Duplicating Center, is that correct?

A Yes.

Q Entry Number 3 is for I.S.Berlin Press, is that correct?

A Yes.

Q Similarly, on the same day, October 18, 1968, you initialed and dated this page, didn't you?

A Yes.

Q The second bill on here -- I am sorry. It is not even a bill, it is a confirmation, it is a confirmation of an account payable. It is addressed to Peat, Marwick, Mitchell, so that it comes back to you.

This is one of the things that you did confirm in writing, is that correct?

A It came back to our office, yes,sir.

Q The person who sent this particular confirmation is the I.S.Berlin Press, is that correct?

A Yes.

Q Does that refresh your recollection as to whether 12 or 13 days prior to your calling up Frank Salgan at I.S.Berlin that you didn't know that they were a printing press?

A Unless I reviewed those papers and I saw I.S. Berlin listed several times, six, seven times, we had a dispute or something, it would be very difficult for me to recall that I.S.Berlin was on the accounts payable papers. I still contend I did not know who I.S.Berlin was as of the date I made those telephone calls.

Q Just so we have all these dates in here, these checkmarks Mr.Stillman showed to the jury are on a page dated October 30, 1968, is that correct?

A That's right.

Q That is twelve days after you did the checking off on those particular ~~confirms~~ confirmations from I. S.Berlin, is that correct? Do I have that right?

A The date between this date --

Q It is 12 days, isn't it?

A It is 12 days between the two papers, yes, sir.

Q I wonder if you would bear with me just a moment,

please, Mr.Scansaroli.

THE COURT: Mr. Scansaroli, while he is looking for papers, it has occurred to me that perhaps I still misunderstand something you were trying to say to my questions and those of Mr.Velie maybe, and perhaps Mr.Stillman.

Were you trying to tell us that your understanding of the method of accounting in vogue prior to Peat, Marwick taking the retainer in the late summer of 1968 was a form of percentage of completion accounting?

THE WITNESS: No,sir. For the year ended 8/31/67 I believe they were on a completed contract basis.

THE COURT: I see. I just wanted to make sure. I thought perhaps maybe we misunderstood you and that you were trying to tell us really the old method, so to speak, was some form or other of percentage of completion accounting.

THE WITNESS: No. I believe they were on a completed contract basis for the year ended 8/31/67.

THE COURT: Did you ever discuss this with that representative of Arthur Andersen --

MR. STILLMAN: Garwych.

THE COURT: -- Garwych?

THE WITNESS: No, sir, I don't believe I did.

THE COURT: Forgive me.

Q In fact, at Page 1970 of Government Exhibit 3

it turns out that on October 23, 1968, only five days after your checkmarks, you noted that you talked to Mr.Frank Salgan of I.S.Berlin?

A That's right. I would think that if I knew that it was a printer I would have inquired as to why we were calling the printer and that it could have been that the printer was doing the work. But at that point in time I did not know that he was a printer.

Q You tell me, sir. What was it that you said to Mr.Salgan and what was it that he said to you?

A I don't recall at this point. I can give you in substance what I said.

Q Why don't you tell us that.

A In effect, on each one of of these telephone calls I indicated that I was Joseph Scansaroli or Joe SCansaroli, I was with Peat, Marwick, Mitchell, we were making an audit of National Student Marketing Corporationfor the year ending August 31, 1968, and that we are confirming certain accounts in connection with this work and that according to my records we have here that you have a commitment with National Student Marketing as of that date for so much money.

That is basically what I said.

Q Do you recall what Mr.Salgan said?

A No, I don't.

I am assuming that everything that I have on that paper is correct, they said yes, they have this commitment, if I indicated on that paper --

End 6B

Q Take a look at this paper and tell me what it was that Mr.Salgan said, Page 1970 of Government Exhibit 3.

A I would have to assume from this paper that he said yes.

Q You are assuming it?

A I have to, that's right. I talked to these people. I would not have left the contract on the books if they wouldhave said no. I would have to say they said yes.

Q I see.

You didn't consider it part of your thorough audit procedure to find out who it was who was on the other end of the telephone and why it was that you were given his number to call?

A I am -- please ask that again.

Q Was it part of this audit procedure you carried out simply to ask who am I talking to and why is it that you have some connection with this commitment? You didn't ask that?

A I assumed it was the ad agency and that is why they would have this commitment. They are working for these companies. It is the responsibility of the ad agency as I understand it. They are working for their clients. They are like an intermediary between their clients and

the people doing the advertising.

Q Did I hear you say that you assumed it was the ad agency?

A I.S.Berlin?

Q Yes.

A I thought it was the ad agency.

Q Rather than do everything you could do, you assumed it was an ad agency?

A I had no reason to believe otherwise.

Q I see. I thought you were auditing this company.

A I was.

Q Let's ask about the Clairol commitment. That is one for half a million bucks, largest one by far, wasn't it?

A Yes, sir.

Q Who did you speak to?

A I believe I spoke to Mr. Zutler. I believe it was Mr. Zutler. I don't recall.

Q Do you remember that as you sit here today?

A I don't recall -- I cannot recall as I sit here today who I talked to unless I look at that paper. I believe it was Mr. Zutler according to that paper.

Q According to what paper?

A Special sales binder.

Q You show me where it says Mr. Zutler on here (handing). I am showing you Page 1970 of Exhibit 3.

A It doesn't say on there.

Q It doesn't? Tell the jury what it does say.

A It says ad agency involved.

Q An agency involved. What was the name of that ad agency?

A I have to look at one of the other documents to see.

Q Help yourself. If you are looking for Clairol, I believe you wll find it down near the bottom. That is my recollection. Page 1969 of that document.

A It says Aaron Zutler.

Q It says Aaron Zutler, contracting officer. What does it say for advertising agency?

A It doesn't say on this paper.

Q Who did you talk to, the advertising agency or the contracting officer?

A If I can recall correctly, I believe it was Aaron Zutler. I can't be sure.

Q You can't be sure. The work paper doesn't help you very much there either, does it?

A In that respect, no, sir.

Q Did somebody tell you that you spoke to Aaron Zutler?

A He told me he was Aaron Zutler, if that is who I talked to.

Q Now yourecall you talked to somebody who said his name was Aaron Zutler, is that what youare telling us?

A I talked to -- if it was Aaron Zutler -- according to that work paper, when I talked to him, he told me he was Aaron Zutler.

Q Let me just see now. As you sit here today, do you have a recollection of somebody telling you his name was Aaron Zutler?

A I can't recall sitting here today, no, sir.

Q I see. In fact, you recall being asked in the grand jury, Page 45: "Do you remember the name of the person you spoke to?

"A No.

"Q Specifically did you speak to a person named Aaron Zutler?

"A I am not sure."

You aren't sure, are you?

A At this point, no.

Q The work --

A Based on those papers, I am assuming on what I

can see in those work papers, I did, but I can't recall the conversation back in October 1968 at this point, no, sir.

Q One of the important functions of work papers, Mr.Scansaroli, is, is it not, to leave a record so that people can find out what it was that you did, isn't that correct?

A The purpose of work papers is to enable an auditor to express an opinion on -- as to the fairness of the financial statements that are being presented.

Q Would you also say that a purpose of the work paper is that it is a permanent record of the work you have done?

A Yes.

Q Allows people to find out what it is that you did do, is that correct?

A To a certain extent, yes.

Q This person, whoever it was that you spoke to about the Clairol contract, can you tell us now whether it was the ad agency or the company?

A Like I said, it was somebody --

Q You can't?

A It was the ad agency. There is no doubt in my mind it was the ad agency.

Q It was the ad agency. All right.

What was the name of that ad agency?

A I can't recall.

Q What was it that you said to the person on the other end of the telephone and what was it that he said to you?

A The same, I can tell you in general terms, the same as the questions that I asked I. S.Berlin. I asked them all the same thing.

Q You just tell us what it was that you said to the people you thought could tell you something about the Clairol contract.

A I indicated who I was, the auditor was Peat, Marwick, Mitchell, they were making an audit as of August 31, 1968, and we were confirming certain accounts. I indicated that I had a commitment on my record that indicated that Clairol had a commitment for $500,000 as of August 31, 1968.

Q You will have to speak up. I am sorry.

A I indicated to the person on the phone that Clairol had a commitment for $500,000 as of 8/31/68. As far as I can recall, that person said that is correct.

Q What was it in your view that National Student Marketing had done to warrant putting down as income for

the year which had ended two months before one-half million dollars?

A As far as we were concerned, the commitments were recorded or should have been recorded as of August 31, 1968.

The commitment was entered into by the client with the account exec prior to that date.

The dates on the documents simply means that the account execs did not send the accounting department the documents on time.

nd 7A

Q Let me ask you a slightly different question. What made you think that 85 per cent of whatever it was National Student Marketing was doing for Clairol had in fact been done prior to August 31, which was two months before?

A We had to accept the account execs estimate in regard to the percentage of completion. There were no time records to indicate that we could check the percentage of completion.

Q Did you check time records, sir?

A No, sir.

Q In fact, you told the grand jury the following --

MR. VELIE: Page 40, Mr. Stillman.

Q --"Those papers are substantially all dated in October", referring of course to Government's Exhibit 3. Is that your recollection, Mr. Scansaroli?

A Yes.

Q "What, if anything, did you do to determine the percentage of completion of work that had been done by August 31, 1968?

"A Nothing. We assumed that these were figures as of August 31, 1968."

Did you tell the truth to the grand jury in that question and answer, sir?

A That's right. I just said the same thing. They did not have records to compute the percentage of completion.

Q So you assumed it?

THE COURT: Would you tolerate ending at this point or am I interrupting you unfairly?

MR. VELIE: I believe we can break at this point, your Honor.

THE COURT: There are several matters I would like to take up with counsel and the litigants. I would just as soon excuse the jury. There's no need to hold them up.

Mr. Lights and ladies and gentlemen, so far as you are concerned we will suspend now until tomorrow morning at 10 o'clock.

Have a good evening.

(Jury absent.)

THE COURT: Gentlemen, if I could have your undivided attention, please, I will try to make this as brief as possible.

First of all, I'm very concerned about the testimony of Mr. Berman in two respects.

First of all, this morning you will recall that Mr. Scansaroli told us that he did not recall either the episode nor did he recall the demeanor or identity of Mr.

Berman at all. At least that's my understanding of his testimony.

MR. STILLMAN: It is, your Honor.

THE COURT: Now, I wonder, therefore, what possible pertinence Berman's testimony has here except, of course, it may well be that there will be later evidence checking him up perhaps, that is Berman, with Mr. Natelli.

MR. STILLMAN: If I may speak to that, your Honor. I think that there is in this record overwhelming circumstantial evidence to reflect the fact that the man that Arnold Berman spoke to was Joseph Scansaroli. May I be heard on that.

THE COURT: You will have to really be heard very forcefully because I see no circumstantial evidence whatsoever to that effect. Berman could not identify Scansaroli at all. Mr. Scansaroli, on the other hand, couldn't identify Berman and couldn't even recall the episode. If that's circumstantial evidence, that the episode occurred with Scansaroli, I must say that I have never heard anything like that since I got out of law school, and I have heard some really strange things around here.

Are you saying there's evidence tying --

MR. STILLMAN: Your Honor -- I will wait until you finish and I will speak.

I say itwith absolute utmost complete sincerity. I point out to your Honor that the evidence in the record reflects the fact that one person and only one person prepared the special sales working paper, that person was Joseph Scansaroli. Mr. Berman testified that the person that he spoke to indicated to him that he was the person who prepared the special sales working papers.

Mr. Berman went on to say there was no question in his mind that the person that he talked to was the person who had prepared the papers.

I submit, your Honor, that that is evidence from which the jury could find that it was Scansaroli that Berman spoke to.

THE COURT: All right. You have answered me. Let me say this, I could also add of course the Government hasn't sought to strike the testimony; those two things.

I will be content for the moment on that. Let me say one other thing which disturbs me deeply. I think it is a monumental unfairness on the record in this case, as I see it. I can't letit go. Our system is under attack enough as it is and I don't want to see any more of it where it is unfair. But it was argued most strenuously to me, as I understand it, that the Government somehow worked an unfairness on the defense by not bringing to the attention of the

defense the name Berman. The alternative understanding I had from all of that was that somehow the Government owed a duty to bring out that they had talked to Berman and so on and so on and Berman somehow was a Brady versus Maryland piece of evidence.

Well, I really find that going a little far even in our far fetched system where free wheeling argument is allowed as it is in the American Criminal Justice System by defense counsel.

I don't see any basis for that at all having listened to Berman. Berman was totally uncertain of too many things.

Mr. Scansaroli, and I have no reason to disbelieve him, was equally uncertain. In fact, he was unequivocal. He had never seen the man that he knew of. He doesn't even recall the episode. I think it is unfair to place on this record and put before a Court a serious application that this somehow amounts to misconduct by the prosecution. I don't follow that at all. I am going to let the record rest at that. I am going to personally blame counsel. I don't think that's necessary.

I do think that there ought to be a forceful statement from somebody here under these circumstances that there doesn't seem to be any content to that kind of accusa-

tion whatsoever now that I have heard Berman and I have heard Mr. Scansaroli.

The second matter, gentlemen, I want to take up with you will be in the robing room and it will not only include counsel, it will also include by my special invitation, the defendants in this case.

Come in.

(In the robing room.)

THE COURT: Mr. Scansaroli, sit down, please.

Mr. Natelli, you sit down.

I want to take up briefly -- and I won't hold you long -- this motion which I received this morning on paper, at least -- of course, you have alerted us to it orally and informally, Mr. Martin -- apparently a joint motion to dismiss the indictment in this case by reason of the statements which Mr. Burton has conceded to the Wall Street Journal reporter, Mr. Andrews.

I am concerned about that in several respects.

Apparently the defendants would seek to have the Court adjourn this trial so that we could persue this issue with an evidentiary hearing. Is that correct?

MR. MARTIN: Not exactly, your Honor. I do think that the motionpaper -- I obviously was waiting for an opportunity to speak directly to the -- does take the position that the only remedy we seek is a dismissal of the indictment. I don'tnecessarily therefore seek to have any hearing that might be necessary at this time. I would be prepared to proceed with this trial and to have such a hearing at the conclusion if necessary.

THE COURT: All right.

That leads me to my next question.

At the very last paragraph of your memorandum you suggest, and indeed, to me, state, among other things, you would like this Court to individually question the jurors as to whether or not they have read the article, which I understood to mean the article which had in it, among other things, what Mr. Andrews purported to say was a quotation from this unnamed source, who we now assume to be Mr. Burton by virtue of what Mr. Burton has told us in his memorandum.

Correct?

MR. MARTIN: Yes, your Honor.

THE COURT: All right. I would like to know no later than tomorrow morning, a few minutes before ten, if you want me to question this jury individually. It seems to me if we are going to do it the only time to do it is as quickly as possible.

However, aside and apart from all these marvelous rules such as Rule 8 of this Court, the marvelous cases which you cited to me, which, by the way, did not dismiss any indictment whatsoever, despite a lot of obiter dictum to the contrary -- I think you will agree that it is only obiter dictum -- and despite everything else we know as lawyers, there is a tactical problem here, and I don't want to ignore it and I don't want to override any possible con-

cerns you gentlemen might have in this regard, and that is why I want the defendants personally to hear this.

I will be glad to, as I have suggested before, but I haven't made it this categorical, of course, individually ask each juror as to whether or not they have seen any article on this case at all. I will be glad to do that. I will of course do it in such a way as to make it clear that I am doing this not at the instance of some specific party or his lawyer. You understand that.

But I want to know now, not later, nto some weeks from now, after the trial is over, because the jury will be disbursed, and I don't want to know it just before we are going to to go the jury, although perhaps -- perhaps -- there would be room for you as a tactical measure to suggest to me, and I would hear it most seriously, maybe you would like me to wait that long. But I want to know which way, and if so, tomorrow morning before we begin.

MR. MARTIN: Judge, I will tell you right now as far as I am concerned. I have thought about this.

THE COURT: You can sleep on it.

MR. MARTIN: Maybe Mr.Stillman and I should confer a little bit.

THE COURT: I want your clients to hear this because I am serious. I am a great believer in trying to comply with the law, but I am also a professional jury watcher, and in my opinion there is a monstrous dichotomy between the written opinions that we all write and the briefs we all write and the cold realities of what in fact goes on in a jury trial in a United States District Court.

You understand me.

MR.MARTIN: Your Honor, I may add, as I say, we have asked for a specific remedy.

THE COURT: I am not prejudicing that remedy. I haven't even gotten to that yet. But I do feel that before I would even consider your motion in chief I have got to know what your position on this is.

You see?

Now, I don't demand an answer now. I purposely wanted to make sure that the defendants were here as well as you so that you could all get a chance to think about it, because I realize there are things to think about, and

I don't blame either one of you or your clients.

I want you to have that opportunity, having heard from me as unequivocally as I can express myself.

Good evening.

MR. MARTIN: Good night, your Honor.

(Adjourned to Thursday, November 7, 1974, at 10:00 A.M.)

United States of America

vs. 74 Cr. 43

Anthony M. Natelli and
Joseph Scansaroli

New York, New York
November 12, 1974 - 10:30 A.M.

(Trial resumed.)

(In open court; jury present.)

J O S E P H S C A N S A R O L I resumed.

THE COURT: Good morning. Mr.Velie.

MR. VELIE: Thank you, your Honor.

CROSS-EXAMINATION (continued)

BY MR. VELIE:

Q Mr.Scansaroli, I believe you told us yesterday it made no difference to you whether National Student Marketing Corporation showed a profit or a loss in 1968, is that what you were telling us?

A Yes, sir.

Q Yet when you wrote down on October 26, 1968, Page 1913 of Government Exhibit 3, your special sales work binder, "If we don't record them," the contracts, "we would probably show a consolidated loss for the year."

You go on to say, "Many of the stockholders will probably wish they had held onto the stock and we could be criticized for not using proper accounting principles."

So you were concerned that if you didn't do it one way or another, you might be criticized?

A At that point when I am analyzing that problem, yes, sir. I had to analyze the problem in light of the whole company.

Q I will read to you some of the information you gave to Mr.Stillman on your direct examination, Page 1495.

"As of this point in time" -- this is Mr.Stillman asking you the question -- "as of this point in time when you were having this conversation with Mr. Randall, had you given any consideration to whether or not National Student Marketing Corporation would show a profit or a loss for the period ended August 31, 1968?

"A I did not focus on it at the time, no, sir.

"Q Did it make any difference to you whether or not this company had a profit or a loss for the year ending August 31, 1968?

"A No,sir.

"Q Has it ever made a difference to you with respect to any client that you serviced while you were at Peat,

Marwick, Mitchell with respect to whether or not that client showed a profit or a loss for a particular fiscal period?

"A No, sir, we worked on so many companies, some would show a loss, some would show a profit. As an accountant it doesn't make too much difference. They are just figures that you are working with."

You gave that testimony yesterday, is that right?

A Yes, sir, I believe it is true. It doesn't make - it doesn't affect me if a company has a profit or a loss.

Q Are you talking about being criticized here?

A I am sorry, I don't think I understand the question.

Q You wrote down, "We could be criticized for not using proper accounting principals."

You were concerned, weren't you?

A In that context, yes,sir.

y I see. I wanted to ask you something else about what you wrote here in Government Exhibit 3. I am reading from Page 1912.

"Under this method extra caution should be used because there is no legal binding contract."

You recall writing that down, don't you?

A Yes, sir.

Q Do you remember yesterday telling me, Page 1603 and 1604, "The extra caution that I was talking about was that the company had to maintain proper records."

A Yes, sir.

Q That was your sworn testimony yesterday, is that right?

A That's right.

Q That is what you were talking about when you said extra caution was needed because there were no legal binding contracts, is that correct?

A Yes, sir.

Q You didn't think that extra caution was required because the clients were not bound to do anything or pay anything to National Student Marketing?

A I am not sure that is a proper statement.

Q The fact is, Mr.Scansaroli, these commitments were not legal binding contracts, were they?

A I am not sure. I would say they were.

Q You would say they were?

A They were oral commitments.

Q All right.

A Oral contracts, yes, sir.

Q All right. They were binding so that the company could collect on them if the client disputed it, is that

correct?

A In my opinion they were, yes, sir.

Q I see. Now I am going to read to you from Government Exhibit 16, which is in evidence.

MR. VELIE: The third page, Mr.Stillman.

(Pause.)

Q If we can all agree the evidence is that Government Exhibit 16 in evidence are the partial notes of the meeting of June 9, 1969, at which Mr. Natelli attended and Mr. Randall attended and some other people that Mr.Kurek told us about at that meeting.

I am reading from what Mr. Natelli said to Mr. Randall on June 9.

MR. STILLMAN: Excuse me. This is the meeting that Mr.Scansaroli did not attend, is that the one?

Yes, I see that. I just wanted to be sure we all understood that.

Q Mr. Natelli is saying, "45 million in sales is fine, but it is important that 3.3 million is unbilled in the balance sheet. Suppose we do run into problems, will you sue them? I doubt if you have got a case. I have got to look at the negative."

Mr. Natelli seemed to have the clear impression that the company could not sue and collect on these binding

contracts.

MR. STILLMAN: Objection, your Honor.

Q Do you dispute that account?

MR. STILLMAN: Objection, your Honor.

THE COURT: I am sorry. I lost a couple of words in there.

Will you read it?

(Question read.)

THE COURT: I think that ought to be rephrased.

MR. STILLMAN: Thank you, your Honor.

THE COURT: Assuming that --

MR. VELIE: Let me try again, your Honor.

THE COURT: You see the point I am making?

MR. VELIE: Yes, sir.

Q You heard what Mr. Natelli was telling Mr. Randall? I just read it to you.

A I heard what you just read, yes, sir.

Q Was that the truth?

A In that memo?

Q Was Mr. Natelli giving a truthful version of what the state of affairs were?

A As of --

MR. MARTIN: I object to the characterization. That is a non-verbatim transcript of the meeting --

THE COURT: Yes, but there is another problem. I think the way to put that, Mr.Velie, is whether or not he would agree that in substance that was an accurate appraisal of the situation at that time as he knew it.

MR. VELIE: Very well.

Q Do you understand Judge Tyler's question?

A I do.

Q All right.

Do you understand what Mr. Natelli is quoted as saying here as being an accurate assessment of the situation at that time?

A I can't -- I can't say that I even focused on that point at any time other than August 31, 1968.

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Q I am going to read to you from your SEC transcript of March 22, 1971, Page 74. Mr. Rowe is questioning. He asks you first about confirmations.

"Q Was it your understanding that the company could book these amounts even if there wasn't a firm confirmation?

"A Yes, sir.

"Mr.Rowe: Whom did you discuss that with, whom in your accounting firm?

"The Witness: We discussed that with everybody involved in the audit, which would include the senior and the partner, although the senior, he would more or less have to leave it up to someone higher than him and he would express his views.

"Mr.Rowe: But those discussions resulted in the decision not to press for written confirmation?

"The Witness: Yes.

"Mr.Rowe: Did you discuss the fact that there might not have been firm contracts at that time?

"The Witness: Yes."

That is so, isn't it?

MR. STILLMAN: Which is so, Mr.Velie? I object to the form of the question, your Honor.

Q Were you asked those questions and did you give those answers to the SEC?

A I am sure I did, yes, sir.

Q You were sworn to tell the truth before the SEC?

A Yes, sir.

Q So you did concern yourself, didn't you, with whether these were or not firm contracts, binding contracts of a legal nature?

A We were concerned -- we wanted to know if they were or not, yes,sir. At that point in time we said that they were firm contracts, that they were binding contracts.

Q You, sir, understood the situation between the account executive and his client to be touch and go, didn't you?

A To a certain extent. That is the terminology I used in my testimony.

Q You thought it was touch and go?

A At that point that is what I used, yes, sir.

Q Let's turn back to the Clairol contract that we had begun to speak about yesterday. Would you tell us please what you determined National Student Marketing had done to earn one-half of a million dollars in fiscal year 1968 with Clairol?

A First of all, they did not earn a half million dollars. They earned the difference between a half million

dollars and the cost.

Secondly, the contracts were being recorded based on the time that the account execs put into these contracts. That was the theory behind recording the contracts on this basis.

Q Will you just tell me then --

A And Ron Michaels, who was the account exec on that contract, had worked on that contract up to a certain point and as far as he was concerned that contract was a good commitment between Clairol and National Student Marketing. He had not finished his work, however. I think we said that he had finished about 85 per cent of his work.

So we recorded 85 per cent of the revenue on that contract.

Q What I want you to focus on is Mr. Michaels' work. What was it that Mr. Michaels had done?

A Mr.Michaels is the same as all other account execs. Their principal duties, if you will, or their principal job was to go out and obtain these contracts from companies, and once this contract was obtained they had very little if anything else to do with that company. Third parties were doing the work, third parties outside of NSMC.

Q You just tell me then if you can what was it that Mr.Michaels did?

A I just told you. His main job or his responsibility was like all other account execs. They were salesmen, in effect. They were going out and obtaining these contracts. They made proposals to the clients, said "This is what we can do, this is the type of programs we have, this is the way we work," that type of thing.

Q Did you ever see a proposal that Mr.Michaels had put together?

A On Clairol?

Q Yes.

A I can't recall, no, sir.

Q Did you ever see a poster or something that he designed or anybody else did for Clairol?

A I can't recall.

Q So he had done 85 per cent of his work in getting a commitment, is that the idea?

A I believe he -- the commitment was obtained. He did 85 per cent of what he had to do on that contract.

Q I see. But you couldn't tell us what it was that he had to do onthat contract?

MR. STILLMAN: I object, your Honor.

A I just told you, sir, the best that I can tell you.

Q That is the best that you can tell us, is that correct?

A I am afraid so. Thatis the way I talk, I guess. That is what it was.

MR. MARTIN: I couldn 't hear that, your Honor. Could we have it read?

THE COURT: Yes.

(Answer read.)

Q Just so that we are all clear on this then, you have no recollection of actually looking at some piece of creative activity or a proposal or a poster or any such thing that Mr.Michaels might have done?

A I can't recall. I saw different materials in his office regarding Clairol but I don't recall what it was.

Q You didn't attach any to your work papers, did you?

A No, sir.

Q You didn't describe any in your work papers, did you?

A I think we described maybe in general terms a program, a poster wave program.

Q What made you think that Mr. Michaels had done any of that work in the fiscal year you were auditing, which had ended two months before?

A This was basically what the company was geared to do. This was their business.

Q I asked you what made you think he did it in the preceding year, sir.

A He did it in the preceding year because he had a commitment as of August 31, 1968. So he had to do it prior to August 31, 1968.

Q Let's just look at the backup for this contract, this half million dollar contract in the file. I have it open at Page 1969 of Government Exhibit 3. This piece of paper is what you put in your work papers here, isn't it, to evidence the half million dollar Clairol commitment?

A This was one of the documents that we had, yes, sir.

Q What else did you put in your work papers? You just show me.

A On Clairol?

Q Yes, sir.

A We had a schedule.

Q Let's see it.

A It is on this schedule here.

Q Just point to it and I will read it.

MR. STILLMAN: What page, Mr. Velie, are you looking at?

MR. VELIE: Mr.Scansaroli has pointed me to Page 1918, in which he has written in pencil "Clairol gross revenue $500,000, account executive $65,000, campus reps $60,000, other $295,000, net to be recognized $153,000."

Q Mr. Scansaroli, this piece of paper you showed me is something you wrote out based, is it not, on the piece of paper we were just looking at a minute ago?

A This was based on Mr. Kurek's schedule.

Q WAs it based on anything from the Clairol Company?

A Let me see what else we have on the Clairol contract.

This here is the Clairol contract. This is the details on -- for a program for one brand on the Clairol contract.

Q You are pointing to Page 1920 in your work papers and again it is something you wrote out in pencil describing something or other. You tell us, please, where you got the information that you wrote down on this piece of paper.

A I got this information from the accounting department of NSMC and from Ron Michaels.

Q These are, are they not, just a listing of the

costs that are on that other schedule, is t' at correct?

A Yes, it shows the gross amount for each contract plus the cost of each brand, for each brand.

Q You will recall that we were inquiring what made you think that they had done anything in August. I want to point to your attention any of these pieces of paper you have here and you tell us what they had done as of August that indicates that the company had earned any of this in the preceding year.

A Yes, sir. I believe in here I made a telephone call to the ad agency and they had agreed that the commitment was made as of August 31, 1968.

Q Is that your testimony? You actually inquired if the commitment had been made in the preceding year?

A The commitment had been made as of -- I was confirming a receivable -- as of August 31, 1968.

Q That is your testimony?

A Yes, sir.

Q Let's just take a look at Page 1969 first. Mr. Michaels dated his backup form on October 17. That is correct, isn't it?

A Yes, it is.

Q It turns out that this program is to take place between January and May of 1969, is that correct?

A Yes, sir.

Q Do you also recall this question and this answer in the grand jury on October 31, 1973, Page 40:

"Q Those papers," referring to these very papers I have been showing you, "are substantially all dated in October. What if anything did you do to determine the percentage of completion of work that had been done by August 31, 1968?

"A Nothing. We assumed that these were figures of August 31, 1968."

Did you give that testimony under oath in the grand jury?

A That's not what we have been discussing,sir. We have been discussing the contract. That had to do with percentage of completion that you just read. That is two different things.

Q What made you think that any of this had been done in August, let alone 85 per cent of it?

A You mean prior to August?

Q That's right.

A I just indicated to you,sir, that the company was involved in this type of business. This was their activity. This is why they were in business, this is why they were incurring expenses, this is why they were

hiring people.

So when I made a telephone call as of August 31, 1968, and the company agreed that they had this receivable, this commitment owing or with National Student Marketing, there was no reason why I should not believe that.

Q You were the auditor, is that correct?

A Yes,sir.

Q You were supposed to keep some independence, is that the idea?

A Yes.

Q Are you confident that you didn't say to some of the people on the telephone something to the effect of "Do you plan to put some of your advertising money into NSMC"?

A Whenever you are talking on the telephone trying to confirm something like this you could have said many things. I may have said to the SEC or the grand jury -- I may have said did they plan, but you are working on words, sir. I am saying we confirmed it as of August 31, 1968.

Q I asked you might you have said something to the effect of "Do you plan to put some of your advertising money in NSMC."

A I may have said that in context with my whole telephone, yes, sir.

Q Mr.Stillman showed your schedule and your checkmarks at Page 1916, as I recall it, of Government Exhibit 3 to the jury. These checkmarks indicate, some of them, that you examined a signed contract or examined a letter of commitment.

Here is a checkmark on Page 1918, green checkmark with a cross through it. It says down here -- that means you examined the signed letter of commitment for Syntex, a total of, according to your schedule here, $138,000 gross revenue to be recorded as of August 1968.

Did you,sir, examine a signed commitment letter from Syntex or did you not?

A If I said I did, yes, sir, I did.

Q You satisfied yourself upon examining that signed letter that it was appropriate to book income as of August 31, 1968,which was two months before?

A Yes,sir.

Q Let's take a look again at Government Exhibit 3. The signed commitment letter you looked at must be this one, isn't it?

MR. STILLMAN: Page, Mr.Velie?

MR. VELIE: 1961, 1962.

Q It says commitment from Syntex, 8/31/68. Is that what you examined?

A Yes, sir, it is probably it.

Q When you examined it during your audit, did you understand that it was dated October 28, 1968, a full two months after the year ended?

A I would say I did, yes, sir.

Q Did you understand that it said, "The following proposal is the result of our meeting last week?" That must have been October 21, 1968, still two months after the year ended.

A Yes,sir.

Q You notice that, too?

A Yes, sir.

Q In examining this thing and reviewing it, did you understand anybody committing himself to spend any particular amount of money?

A I don't think there is any definite amount in this commitment; no, sir.

Q Any definite amount? There is no amount at all, is there?

A No, sir.

Q It doesn't seem to speak too clearly, does it, of what it is that National Student Marketing is going to do anyhow, does it?

A I would say no. There is no specific

program as such.

Q In fact it looks like they are going to begin their work some time after October 28, doesn't it?

A Which isn't unusual, yes, sir.

Q And finally there is a money back guarantee in here, isn't there?

A I don't know, sir.

Q You don't know? I thought you reviewed it. Why don't we just read it aloud together. It says here on Page stenciled 1962, "The contract we developed and the guarantee that we discussed at our meeting will be outlined in detail. At this time let is suffice to say that any moneys spent on the direct mail program will be recovered by Syntex or NSMC makes up the difference."

That is a money back guarantee, isn't it?

A Yes,sir.

Q So there is no assurance whatever that National Student _Marketing will ever get paid anything for this, is that right?

A Based on that language being very specific, yes, sir.

Q And that was the signed commitment letter that you reviewed in your audit backing up $138,000 worth of

a commitment?

A I don't recall the amount of the commitment.

Q Otherwise I have stated it accurately?

A Yes,sir.

Q Mr.Scansaroli, to say the least, your oral and other audit procedures were not customary, were they?

A I would say in total they were not customary, no, sir.

Q In fact, oral confirmations are not normal,are they?

A I haven't had that much experience with oral confirmations. I have made oral confirmations, however.

Q Would you say they are not a normal method of confirming?

A In most cases that is right, yes.

Q In most cases they are not normal?

A That is right.

Q In fact, sir, your audit was wholly unusual and unprofessional, wasn't it?

A I don't think I could agree with that, no, sir.

Q Do you deny that you were far too easily satisfied in your audit?

A Based on what I know now? At that time,sir, I did the best job that I could do based on what I saw,

based on the facts that we had at hand, based on everything we did. I satisfied myself that what we did, those commitments were proper.

Q I asked you, do you deny that you were far too easily satisfied?

A Based on all the subsequent facts and sitting here as of today, I would reflect on it and say yes.

Q Yes?

A Yes.

Q In fact, a little earlier than today you had an opportunity to reflect back on whether you had been far too easily satisfied, didn't you?

A I may have said at the SEC, yes, sir.

Q Only six months after allthis income was booked over a million dollars got written off?

A That was a very unusual circumstance, sir.

Q These commitments were highly material, weren't they?

A Yes,sir.

Q They were the difference between a profit and the loss for the company for the year, weren't they?

A I believe so, yes,sir.

Q You do believe that?

A Yes, sir.

Q Then you don't dispute Government Exhibit 65-2 which shows what you reported, handsome gains for the year with the unbilled --

MR. MARTIN: I object to the characterization, your Honor.

THE COURT: I am sorry. You object to what characterization?

MR. MARTIN: In Mr. Velie's question, handsome.

THE COURT: Handsome, I missed that I am frank to say. Do you mind deleting the word "handsome"?

Q Mr.Scansaroli, this chart then, you don't dispute it, it shows $388,000 of after tax profit for National Student Marketing with unbilled accounts receivable and a $65,000 loss without them? That's about right, isn't it?

A Put in that manner, yes,sir. I think it is an unfair chart.

Q However, you don't dispute what it shows? There is a loss without these contracts?

A I would say that is close, yes, sir.

Q You would say that is so, is that right?

A Yes.

Q We have already learned from you that there

substantial dangers that National Student Marketing might never receive the income that you anticipated in those contracts, is that true?

A I never said that, no, sir.

Q Well, let me just see about that. You recall Judge Tyler yesterday asking you this question, Page 1505:

"On the other hand, would it not be fair to say from your professional viewpoint that in order for percentage of completion method of accounting to work, that presupposes complete and accurate records of work in progress and accounting or financial records relating to each one of the contracts or deals?

"A Yes, sir.

"The Court: And absent those data, the percentage of completion method becomes somewhat chancey and ineffective from an accounting point of view, is that a fair statement?

"The Witness: Yes, sir."

And you have already told us, have you not, Mr. Scansaroli, that there were no appropriate records for these contracts?

A The records were not what they should be.

Q You wrote down on October 23, 1968, Page 1970 of Government Exhibit 3, "Accounting, bookkeeping and

maintenance of files was almost forgotten. This was especially true in the area of contracts, account executives and other files and data with regard to gross income on contracts."

You wrote that, didn't you?

A That is not the same as your question, sir.

Q Is that your explanation?

A Yes.

Q We have already seen, haven't we, that you wrote down that extra caution should be used because these were not legal binding contracts, is that correct?

A Referring to the client must use extra caution and making sure they had proper detailed records.

Q I see.

You weren't concerned that there was a problem in collecting these since the company couldn't sue in court? That was not your concern?

A No, sir. I never said they couldn't sue in court.

Q This was the first year that National Student Marketing had ever had operations of this kind on this scale, isn't that true?

A Yes.

Q Work hadn't been performed yet, is that true?

A No, sir. I keep tellingyou, it depends on what you mean by work. The account executives, their work was completed or a percentage of it was completed.

Q National Student Marketing couldn't get paid until they tacked up the posters or sent the mail, isn't that true?

A Yes.

Q They hadn't done that yet, had they?

A As of August 31, no, sir.

Q As of October when you booked these things, had they?

A No, sir.

Q You had no real assurance that they had the capability to do that, did you?

A I never doubted it.

Q Is it that you didn't doubt it because you didn't know the contract guarantee provisions?

A I did not know the guarantee provisions, but I believe they were very few, if I am not mistaken.

Q There were very few writings underlying the commitments, that is why there were very few guarantee clauses, isn't that true?

A I don't think I could put the two together, no, sir.

I am saying that most of the company's contracts did not have guarantees that I can remember.

Q Did you inquire whether there were guarantees?

A No, sir.

Q I see.

I believe you have alreadytold us a few times that the situation was touch and go between the salesmen and the clients.

A That is one of the words I used at the SEC, yes, sir.

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Q Were those words untrue?

A Well --

Q Do you wish to change that testimony?

A It depends on what context. I say, that is what I said at the SEC. I am not saying it is not true.

Q You kept Mr. Natelli informed of all of these factors, didn't you?

A What factors, sir?

MR. STILLMAN: Objection to the form of the question, your Honor.

Q Do you understand my question, Mr.Scansaroli?

A No, sir.

Q Did you keep Mr. Natelli advised of the fact that commitments were highly material in that there would have been a loss without them for the year?

A It was in the memo.

Q Did he review the memo?

A I believe he did. I am not sure.

Q Did you therefore inform Mr. Natelli because of your memo that there were problems with the files that were being kept or not being kept?

A I didn't say there were problems. I just said they didn't have a sufficient number of files, they could have had more.

Q Did you inform Mr. Natelli that there were no legal binding contracts?

A According to that memo, that is what I wrote, yes,sir.

Q Did you inform Mr. Natelli that this was the first year National Student Marketing had tried operations of this kind on this scale?

A We were all aware that National Student Marketing was a growing company.

Q Were you aware of that, was he aware of what I have just read to you?

A If he read my memo.

Q The two of you were aware that National Student Marketing had not yet performed the work which they would be required to perform in order to get paid? That is true, isn't it?

A Yes,we knew that.

Q I guess you have told us you didn't know about the guarantee clauses and didn't check, so you didn't tell Mr. Natelli?

A That's right, we weren't aware of any guarantee clauses.

Q Did you tell Mr. Natelli that the situation was touch and go between the account executives and the clients?

A I don't think I ever told him anything like that, no, sir.

Q In April, Mr.Scansaroli, only six months after these contracts were booked and the annual report went out, six months later, you learned,didn't you, that of the $1.7 million of these contracts over $1 million of them were written off as no good and uncollectible?

A I know that the Ron Michaels contracts had to be written off. I believe it was in April some time.

Q You weren't aware of other writeoffs?

A I was aware of other writeoffs but not in that context. I reviewed the work papers as of -- for the period ending February 28 and I indicated on that work paper that there were certain writeoffs. But the majority of that $1 million was the Ron Michaels contracts.

Q Let's just focus on this. Didn't do an SEC review looking toward a proxy statement that was to be issued with the February figures in it?

A Yes, sir.

Q In connection with that SEC review did you gather together various items of information about these contracts?

A We had schedules, yes, sir.

Q On May 22, 1969, did you staple this schedule,

Page 2618, into your proxy binder?

A Yes.

Q It shows $345,000 of contracts already written off by the company, is that correct?

A Yes, it did.

Q That only includes one of the Ron Michaels contracts, is that correct? It includes Listerine in the amount of $70,000?

A Yes.

Q So the great majority of that $345,000 of contracts were written off and you knew about it in May?

A In May, yes, sir.

Q In addition to these you yourself wrote off an addiitional $678,562 worth of contracts on May 12, 1969, only ten days before?

A Those are the Ron Michaels contracts, yes, sir.

Q Check my arithmetic, if you would. That is over $1 million, isn't it, the 678 plus the 345?

A In total sales, yes, sir.

Q At Page 2619 of your SEC review appears an analysis of the contracts written off by the company, is that correct?

A Yes, sir.

Q A salesman by the name of Ganis is responsible

for about one-quarter of a million dollars of these, isn't he?

A 226,000.

Q That is pretty close to a quarter of a million dollars, isn't it?

A Yes,sir.

Q In addition to the ones written off you yourself had questions about the Faberge?

A Yes, I asked questions about those and wrote the answers.

Q You wrote down no contract, right?

A Right, change from spring to fall, no contract.

Q You did that on May 22, 1969?

A Well,I am not -- I probably did it in May some time. I am not -- I probably did it in May some time. I am not sure.

Q You stapled it into your book on May 22?

A Yes, sir.

Q The Campana contract, you wrote down writeoff, is that correct?

A Yes.

Q The Pace contract, you wrote down writeoff, is that correct?

A Balance of $14,992 should be written off, yes.

Q You wrote down Syntex, writeoff?

A Yes.

Q Weren't you startled?

A No,sir, I wasn't.

Q Didn't you just say that this was unusual?

A No, sir, I didn't. May I tell you why? You are taking things out of context. You have got to remember that we are working along for month after month after month.

You have had time for the last six months to a year to pull things out and put them in the spots that you wanted. We didn't operate that way. We had to make decisions on a daily basis as we were going along. We did the best we could. Certain contracts had to be written off, we told the clients to write them off. The clients said they were good contracts, they were good contracts.

We did not have the luxury of hindsight to sit there, put things on charts, put things -- take things out of context and say here is what the picture is. We didn't have that type of picture. We had to do it on a daily basis as we were going along.

Q Sir, in ten days in May you noted the writeoff of well over $1 million of those contracts --

A You keep saying $1 million. I agree with you. But I am saying most of that was the Ron Michaels contracts.

You keep harping on the Ron Michaels contracts. We all know what that was. We know why it was written off. We know that Ron Michaels acted unethically. Why do we have to keep bringing that up? We all know it now.

Q Another half million dollars was not Ron Michaels, is that correct?

A I don't recall. It was like two, $300,000 in gross sales, I believe, something like that.

Q You told us you had done everything possible, except for some fine points, to check these contracts, is that correct?

A As of when? As of August 31, 1968, yes, sir.

Q Didn't that make you think that your audit might have been insufficient in some way?

A No,sir.

Q It didn't. Just tell me, wasn't this an item, the fact that $1 million of your sales had been written off of $1.7 million within a six month period, you learned of it all within a ten day period, didn't this shed some light on events since your audit?

A Mr.Velie, it did not, simply because of the fact that when you are working there youare working on a daily basis, you are working hard, you are putting figures

together, and all of a sudden someone comes in and says that Ron Michaels in effect took kickbacks, his contracts were no good. You are talking about one major item in this whole thing. That is where most of your million dollars is. You just don't look at it from the standpoint you are looking at it.

Q You told us you were working on a daily basis?

A Yes, sir.

Q On May 22 did you sign off on your SEC review checklist?

A I don't know when, but I did, yes.

Q You certainly stapled it into your book onMay 22?

A Yes, sir.

Q And Item No. 5 --

A Not on May 22.

Q You stapled it in here?

A I stapled it in, yes, sir.

Q That is the day you stapled a lot of other things in here.

A I guess so.

Q Item 5 says "Inquire into all matters raised at the time of our audit on which the lapse of time might shed some additional light." That is what it says, doesn't

it?

A Yes.

Q On May 22, 1969, did this shed any light on you, the $1 million writeoff?

A I don't think I understand the question, sir.

Q On May 22, 1969, was any light dawning on you about your audit?

A No,sir.

Q Had you lost your fear of being criticized for using improper accounting practices which you noted in October of 1968?

MR. STILLMAN: Objection to the form of the question, your Honor.

THE COURT: Sustained as to form.

Q In October of 1968 you wrote down a concern about being criticized for using improper acoounting practices. Do you recall that?

A I said we would be criticized if we did not do the proper thing at that time.

Q Six months later had you lost a concern about being criticized for doing improper accounting with respect to this company?

A Whenever you are making a decision on accounting

you always try to do what is right, the best possible approach, and that is what we did all along.

Q Did you lose your concern, sir, about being criticized?

A I don't know what you mean by did I lose my concern about being criticized. Criticized about what?

Q About not using proper accounting practices.

A In what respect?

Q In respect to the fact that you allowed the company to put $1.7 million of accounts on after the period had ended, switching a large loss into a dramatic gain, and that within six months one million of them had been written off and none of the rest to any large extent had been seen to be collectible.

A Mr.Velie, I didn't say that in my memo. Did I say that in that memo? You know I didn't say that. You are taking words out of context again.

Q Is that your explanation?

A Yes, you better believe that is my explanation.

Q So what is it now, you weren't concerned in the first place?

MR. STILLMAN: Your Honor --

A I am sorry, I don't understand the question.

MR. STILLMAN: He is inviting argument by this kind of tactic.

THE COURT: Just a moment. I take that as an objection as to form, which I sustain.

Q Let's just take it piece by piece. Were you concerned in October or weren't you concerned about being criticized?

A I am sorry, sir. Criticized about what?

Q I am just going to read this to you, your own words, and ask you whether they accurately reflect what it was you were saying:

"We could be criticized for not using proper accounting principles."

Was that a concern of yours in October when you wrote this?

A That was a concern with regard to that matter, yes, sir.

Q The matter being the unbilled accounts receivable, is that correct?

A Regarding on what method to record them.

Q Did it occur to you six months later that maybe the wrong method had been chosen, when all these facts came to light?

A No,sir.

Q As a general proposition, did you lose your concern for being criticized with respect to unbilled accounts receivable choices?

A Sir, I was never worried about being criticized about anything in the sense that you are saying.

Q Sir, you heard Mr. Kurek testify here from that chair you told him you were concerned about the commitments. Is that the truth?

A I don't recall that conversation, no, sir.

Q You told him you didn't know whether the right decision or the wrong decision had been reached back in August. He said that. That was the truth, wasn't it?

A I don't recallthat conversation, sir. We discusse a million and one things during this period of time.

Q He testified that you were concerned about your CPA certificate. That was the truth, wasn't it?

A I was never concerned about my CPA certificate at any point in my life. From the time I received my certificate until we finished this thing I never even gave that a thought, never.

Accountants don't work that way. Even if you do make a mistake you don't lose your certificate for making a mistake.

End 4

Q Mr. Kurek testified that you said you would have to put your certificate in a locked box in the bank. Do you deny --

A He testified to that. I didn't know what a locked box was until two days after he testified.

Q You told Mr. Natelli you were concerned you would lose your CPA certificate, didn't you?

A I don't recall making that statement, no, sir.

Q Do you deny that that's the truth?

A I don't recall making that statement, sir.

Q Do you deny that that is so?

MR. STILLMAN: Asked and answered, your Honor.

THE COURT: No, I don't think so.

MR. VELIE: He hasn't answered.

A Do I deny I ever made that statement?

Q Yes, sir.

A I have to deny it, yes, sir.

Q Government's Exhibit 14 in evidence, I think we can agree this was identified by Mr. Kurek as a memorandum of June 3, 1969 he wrote to Mr. Randall about a meeting, June 3, 1969. Tell me, Mr. Scansaroli, how many days between May 22 and June 3?

A Approximately 11.

Q Less than two weeks?

A Yes, sir.

Q "In re: Meeting with Tony Natelli. I met with Tony this morning from 9:30 to 11 incidental to our phone conversation yesterday.

"Kurek of course meeting with Natelli.

"I reviewed with him the progress our profit planning and budgets were making" he goes on to discuss that.

"After discussing the above and setting the atmosphere of the meeting, the subject of the meeting was changed to that of NSMC manner of booking contracts. Tony is very concerned about the situation. Last fall he felt that the manner in which he allowed us to book contracts would be a cyclical deal. In other words, we would be selling and delivering on contracts at the same quarter that financial reports were made. He now says the situation was one where commitments either make or break us and we are not performing in the period the sale is made. Furthermore, he anticipates that unbilled receivables could be as high as $4 million at August 31, 1969. If so, he will have to give us a qualified opinion or no opinion. This is very serious since it could adversely affect our registration that fall. He stated that people working under him are uncomfortable with this situation and if anything were to happen,

their certificates and careers would be at stake."

You were working under Mr. Natelli, weren't you?

A Yes, sir.

Q You were the man who did all, all of the auditing work on the unbilled accounts receivable, is that correct?

A As of when, sir?

Q As of August 31, 1968, $1.7 million of unbilled accounts receivable?

A Yes, just about all.

Q You were the only one. A million dollars of the contracts you checked got written off?

A Yes, sir, that includes the Ron Michaels contracts.

Q Mr. Natelli had reference to a conversation with you then, didn't he?

A I don't know, sir. If he says he did, he's an honest man, I will agree with him, but I don't recall it.

Q A moment ago you denied it.

A I denied it because I don't recall it. I have to deny it.

Q Another interesting thing happened on May 22, 1969, isn't that right, Mr. Scansaroli?

MR. STILLMAN: Your Honor, the form.

A I don't know, sir.

Q On May 22, 1969, this is your paper in the proxy binder?

MR. STILLMAN: The page you are looking at, sir?

MR. VELIE: 2623.

A That is my initials on the work paper. I stapled this in, yes, sir.

Q On May 22, 1969, the day all this other information was coming about, you stapled in the Pontiac commitment in over a million dollars, is that correct?

A Yes, sir.

Q That Pontiac commitment is a commitment once again for the period which had ended some months before, isn't that true?

A I believe it was for the period ending February 28, 1969.

Q It was for the period ended February 28, 1969, and the letter is dated April 28, 1969, is that correct?

A Yes, sir.

Q Did you think it an odd coincidence that a $1.2 million contract came in after the period just as $1.2 million of unbilled accounts receivable went out the window?

A No, sir.

Q You didn't think that?

A No, sir.

Q You mentioned these Michaels contracts, didn't you?

A Yes, sir.

Q The ones you permanently wrote off amounted to ~~of~~ $678,000, is that correct?

A Yes, sir.

Q In addition, there was another Michaels contract in the amount of $70,000, is that correct?

A Yes, sir.

Q The company wrote that one off?

A According to our work papers, I wrote it off.

Q It appears on your schedule at 2618 as already having been written off?

A Yes, sir.

Q All right.

You told us something about a kickback yesterday, Mr. Michaels you say had received a kickback.

A That's what we were told, yes, sir.

Q What were you told?

A I was told that Ron Michaels had received kickbacks and that his contracts were no good.

Q You had audited those contracts, hadn't you?

A Yes, sir.

Q I see.

Who told you that Ron Michaels had received a kickback?

A Mr. Randall, I believe told Mr. Natelli and Mr. Natelli told me.

Q Mr. Natelli told you?

A Yes, sir.

Q Mr. Scansaroli, Michaels was being used as the scapegoat to absorb all the blame for these contracts, wasn't he?

A No, sir. Not that I -- You say that. I don't think so, no, sir. I don't even know the circumstances behind all this.

Q Did you check to see if Mr. Michaels had done anything wrong whatever?

A No, sir.

Q Did you check to see if any of these other contracts that had gotten written off were the result of something improper?

A No, sir.

Q I think you already noted a salesman by the name of Ganis was responsible for about $226,000 of the write off?

A From that work paper, yes, sir.

Q You didn't check him, did you?

A No, sir.

Q Can you see the board?

A Yes, sir.

Q That's the amount, isn't it, $678,000 that you wrote off of the Michaels contracts?

A That's the gross amount, yes, sir.

Q Gross amount.

Absorbed with that was exactly this amount of costs, is that correct?

A Yes, sir.

Q So we have $678,562 exactly of contract revenue and $489,812 exactly of contract costs. If we were to subtract that we would get exactly $188,750 of profit to be written off, is that correct?

A Yes, sir.

Q All right.

You told us about a tax credit.

A Yes, sir.

Q You and Mr. Natelli computed the tax credit, didn't you?

A As of August 31, 1968?

Q No, as of the discovery of the new tax credit.

A I believe that the Tax Department -- I believe the Tax Department informed us of it.

Q Who computed it?

A In May? I believe it was the Tax Department.

Q You do?

A Yes, sir.

Q The SEC transcript, April 12, 1971, page 221 and 222.

"Is there anyone that would have been associated with the job that understood this item?

"A Well, I'm not sure anybody would understand until they went back and reviewed all the figures again. I believe at this time Tony Natelli and I were the only two that really got involved in it.

"Q Did you understand this item?

"A At that time, yes."

Q Would you like to look at this and satisfy yourself?

A No, I agree with you, sir.

Q We are all talking about the tax item?

A Yes, sir.

Q You and Mr. Natelli were the only ones who knew about it and the only ones who computed it?

A No, sir.

Q You didn't tell the truth to the SEC on that matter?

A I told the truth to the best of my recollection at that time.

Q You recall it better now?

A Yes, sir.

Q You heard Carol Raimondo come in and say she didn't compute it. You say she computed it?

A In effect, she computed it.

Q You disputed her testimony?

A In effect, she told me no liabilities should have existed as of that date. That, in effect, is the same as computing it.

Q Tax deferral accounting is a fairly complicated matter, isn't it?

A Yes, sir.

Q You did some computations?

MR. STILLMAN: Fix a time.

Q When you came up with the new credit.

A I don't think we did any computations, no, sir. There was no computations that had to be made.

Q Bear with me a second, please.

THE COURT: Perhaps --

MR. VELIE: Just this brief piece, your Honor.

THE COURT: All right.

Q There's a question, page 248 of what the 188,750

tax credit consisted of .

"A Yes. We worked on it -- like I said, it should have been a separate entry regarding the tax calculation, and, I am surprised -- there's no work paper. I should think there would be a work paper somewhere?"

Do you recall that testimony?

A SEC testimony?

Q Yes, sir.

A YEs, sir.

Q Does that help you with respect to whether you did some computations and there might have been a work paper?

A I'm saying at this point now what I know. There could not havebeen any computations. It was the obvious fact that was on the books did not belong on the books. It didn't need to make a computation. The difference -- the computation was just taken from the books, taken back off.

Q When you went in the SEC, you took a recess to search for the work paper, didn't you?

A That's right, sir. I did not have to look at any of the work papers. You said yourself that the deferred tax is a very difficult situation. We had a lot of problems in deferred tax from the time of that point in time until we were reviewing with the SEC in letters in 1970. To him things have happened. You can't answer that type of question

without looking at the work papers.

Q There is no work paper, is there?

A I just told you no, sir. You didn't need one.

Q You just rounded off, to use your term, tax credit, computed it in your head to an amount exactly equal to absorb the loss on the Michaels contracts you were writing off, is that correct?

A Please repeat the question.

Q You used the word rounded off yesterday, is that correct?

A Yes, sir.

Q So you just rounded off whatever this tax figure was that you had computed in your head without a work paper to exact an amount sufficient to absorb every penny of the loss being written off?

MR. STILLMAN: I object, your Honor.

THE COURT: Overruled.

A We rounded the tax computation off to that figure. That's right. We could have increased the income by another 20,000, but we left it in as a cushion.

MR. VELIE: Could we take our break at this time?

THE COURT: Yes, sir. We will take the morning recess, ladies and gentlemen. Ten minutes.

(Recess.)

THE COURT: Anything else, Mr. Velie?

MR. VELIE: Yes, your Honor.

xx BY MR. VELIE:

Q Mr. Scansaroli, there was no tax credit in the amount of $188,750 after all, was there?

A You mean tax adjustment?

Q Yes, sir.

A There was at that time, yes, sir.

Q Later on it turns out that that was wrong, is that correct?

A In 1970 we determined it was wrong, yes, sir.

Q You determined it was wrong after the SEC began an inquiry, is that correct?

A That's when we reviewed it, yes, sir.

Q So you made a mistake?

A Yes, sir.

Q Incidentally, you told us a little bit about deferred tax accounting. Was it you or was it Mrs. Raimondo? I have forgotten. Did you tell us about deferred tax accounting yesterday?

A I don't recall, sir.

Q It turns out National Student Marketing reports to Uncle Sam different information than it reports to the public, is that true?

A Yes, sir. It is nothing unusual.

Q Just so we get in this context, is it not so that the tax adjustment or tax credit, if you will, being talked about here, the one that you and Mr. Natelli computed, that tax credit results from a net operating loss carried forward? Do I have that right?

A Yes, I believe that's what happened.

Q That simply means, doesn't it, that in 1968 National Student Marketing told Uncle Sam it had a loss, is that right?

A Yes, sir.

Q In 1967 National Student Marketing told Uncle Sam they had a loss, is that right?

A I believe so, but I am not sure.

Q The same for the predecessor years, is that correct?

A I don't know.

Q If there had been a gain in a prior year you could have carried the credit back, is that correct?

A To the extent of the gain, yes, sir. What you don't carry back then you carry forward.

Q But you do have a recollection of tax losses in '67 and '68?

A Yes, sir.

Q Mr. Scansaroli, you remember this, don't you? It is in evidence as Government's Exhibit 17B and this is chart 65-10.

A Yes, sir.

Q You were the accountant, were you not, who in fact took numbers from the work papers and put them into the footnote as it appears in the text, is that correct?

A I am not sure if it was me or somebody working with me. I would have to look at the work papers to see.

Q You want to look at Exhibit 13? Would that be a help to you?

A I would have to look at the draft of the -- you have to have a draft of the original report. I could have put those in or somebody working under me could have put the figures in.

Q Let me just ask you a few questions about it. This line that says "Pooled companies reflected retroactively," with the number $6,389,000 some odd, that is not the true figure for the sales of the pooled companies reported on this line, is it?

A No, sir.

Q Somebody subtracted $678,000, the Michaels contracts, which are National Student Marketing losses, somebody subtracted that from the pooled companies?

A They reduced the sales by that much, yes, sir.

Q You did it, didn't you?

A I don't recall if it was me or somebody with me.

Q Do you deny doing it?

A Sir, I don't recall.

Q If you had done that wouldn't you recall it?

A No, sir. We were working with thousands and thousands of figures in those days, with that proxy statement.

Q Your explanation is that that might have been a mistake, is that the idea?

A No, sir, I don't think so. What would have been a mistake?

Q To subtract $678,000 from National Student Marketing's losses from these other companies that National Student Marketing gobbled up in the succeeding year?

A Well, I don't think, first of all, those are losses, and they didn't gobble these companies up, sir. I just don't understand your question. It is an immaterial item in relation to total sales for that year.

Q It is immaterial. Well, would you say that $1 million is a material item?

A What was the total sales for the year?

Q $5 million.

A The total of consolidated sales on the proxy statement.

Q Let's talk about National Student Marketing sales in 1968.

A You can't do that, sir. You have to talk about the whole company. It is one company. You can't look at part of a company. This was one company as of that date.

Q In 1968 --

A That's not 1968 figures in that proxy statement.

Q It isn't.

A If you look at the proxy statement that will show the 1968 figures.

Q You have the annual report right in front of you, don't you?

A This is not the same figure that was in existence as of the date that proxy statement was prepared. It is not the same company.

MR.VELIE: Your Honor, I ask for a direction to the witness to answer my question.

MR. STILLMAN: Your Honor, I submit he has an answer to his question.

Q The question is that the 1968 report sitting in front of you, Mr. Scansaroli.

MR. STILLMAN: Of course it is.

A Yes, it is.

Q Very well. Will you please turn then to the figure for sales for 1968 as reported to the public.

How much?

A As of this report it was $4,989,446.

Q $4,989,446?

A Those are the net sales, but there are also --

Q That is what is here, net sales originally reported, $4,989,446.

A Yes, sir.

Q At least $1 million of those were written off, is that correct? You knew about that?

A The Ron Michaels contracts.

Q I asked you was not $1 million of those sales written off within six months after you reported them to the public?

A They were written off -- let's see. I am not sure of six months. Six to nine months.

Q Your report didn't come out in August, did it?

A This --

Q The annual report for 1968.

A This annual report was dated in November.

Q It is dated in November. The write offs were in April and May, isn't that right?

A '69, yes, sir.

Q It is about six months, isn't it?

A From the date of the report?

Q Yes, sir.

A Yes, sir.

Q $1 million had been written off, is that right?

A Yes, sir.

Q This is the final proxy. No disclosure anywhere, is there, that $1 million of the $5 million originally reported was written off, is that correct?

A No, sir, there is not.

Q There is no disclosure. It turns out also that somebody has subtracted three quarters of a million dollars of that loss not from the sales originally reported but from the pooled companies which were acquired later. That's so, isn't it?

A Going from the original sales to the sales per the proxy statement, that's right.

Q So the pooled companies are understated by three quarters of a million dollars, is that correct?

A Yes, sir.

Q National Student Marketing is over stated by three quarters of a million dollars at least, is that correct?

A In that context, yes, sir.

Q No disclosure anywhere that this is happening, is that correct?

A We didn't think a disclosure was needed, that's right.

Q That is exactly what paragraph 3 of the indictment charges, is that correct?

MR. STILLMAN: Objection.

THE COURT: Yes. I am going to sustain that.

Q Just so there is no confusion, you understand this particular footnote to be the footnote which is the subject of paragraph 3 of the indictment, don't you?

A Yes, sir.

Q If I understand your explanation for the non-disclosure, it is, is it not, that because of the tax credit of $188,000 the net amount in the earnings portion of the footnote is only $21,000, is that correct?

A Yes, sir.

Q You knew about APB No. 9, didn't you, Mr. Scansaroli?

A Yes, sir.

Q You heard Mr. Dingwall's testimony about it?

A Yes, sir.

Q Were you aware that APB No. 9 says "Even though

material extraordinary items may net to an immaterial amount there should be positioned and disclosed as follows: The income before the extraordinary items, the extraordinary items separately, and then the net income."

A Was I aware of that at that time? No, sir.

Q You weren't aware of that?

A No, sir.

Q But you were aware of APB No. 9?

A Yes, sir.

Q Were you aware of this, sir, also in APB No. 9.

"Whenever prior period adjustments have been reported" --

MR. MARTIN: Will you read the start of the sentence.

Q "The Board further recommends that whenever prior period adjustments have been reported during any of the periods included therein the reported amounts of net income and the components thereof as well as other affected items be appropriately restated."

Were you aware that that was the rule?

A I believe I was, yes, sir.

Q You believe you were?

A Yes, sir.

Q The components of this restatement include a

three-quarter of a million dollar sales write off. Where is that disclosed?

A It is not disclosed because the net effect in our opinion was immaterial. We started to disclose this --

Q It said the components, didn't it?

A That's what that says. If you let me tell you what happened I can tell you why it was not disclosed.

Q Let's just see if we have it now. One of the components was three-quarters of a million dollar sales write off, is that correct?

A Yes, sir.

Q The second component were the costs associated with it?

A Yes, sir.

Q The third component was the income being written off?

A No, sir, the third component was the tax.

Q No income was written off at all?

A That was not a component. The three components were the receivable, the payable and the tax liability. Those were the three components.

Q Wouldn'tyou think that it would be interesting to know if you are reading an income statement where a company's earnings are made up of its sales or made up of a

tax loss?

A In this situation, no, sir. It was immaterial. We are talking about in 1968, for the year ending 1968 -- I don't know what the income was -- and for the nine months ending May 31, 1969 you are talking about $700,000 net income. The net effect is $21,000. Are you trying to tell me the reader of that financial statement would care about that $21,000?

Q Wouldn't the reader of the financial statement like to know that the $1 million had been written off?

A Not when you have a total of something like $11 million. It was not material.

Q Wouldn't that reader like to know that $2 million of 3.3 million recorded over an 18 month period had been written off?

A No, sir.

Q Wouldn't like to know that either?

A No, sir. The complexity of that company changed so much in six or seven months that it was immaterial.

Q Some of the people who might be reading that proxy statement had already been acquired, had their companies acquired by National Student Marketing. Don't you think they would like to know if the statements that they relied on in 1968 had turned out to be utterly no good?

MR. STILLMAN: Your Honor, I submit that this is a direct violation of a previous ruling that you made on this subject. There is no charge in this indictment that anybody was defrauded as a result of what is in that proxy statement.

MR. VELIE: I disagree with that.

THE COURT: I don't think the question is quite susceptible of that simplistic interpretation. Go ahead.

Q Do you understand my question, sir?

A Read it back, please.

Q I will put it for you again. Some of the people who might read that proxy statement had given up their little companies --

MR. STILLMAN: Your Honor, they got millions of dollars. How could he talk about little companies?

MR. VELIE: Mr.Stillman,you take the oath and get on the stand.

MR.STILLMAN: Forgive me. I apologize.

THE COURT: I would agree with you, however, to this extent, that we don't have to characterize the companies in any way. Little, big, medium is unnecessary, Mr.Velie. You just don't have to do it that way from your viewpoint.

MR. VELIE: Yes, your Honor.

Q Some of the people reading that proxy statement had given up their own businesses and received in exchange National Student Marketing stock, is that correct?

A Some received stock, yes, sir.

Q And they had been relying on in understanding whether that was a good deal or not Government Exhibit 5, the annual report for 1968, is that right?

A Some companies rely on some of the figures in

the proxy statement. It depends on when the company was acquired.

Q Some relied on the 1968 report as well, is that true?

A They had it. Whether they relied on it, I don't know.

Q Others were relying on the proxy statement you just said?

A Other companies in the acquisition had the proxy statement.

Q And they were relying on it?

A Whether they would rely on it, I don't know. It is a very complex proxy statement. I doubt very many people looked at it.

Q You doubt that anybody looked at it?

A I doubt many people looked at it or would understand it.

Q I see. There isn't a hint in that proxy statement anywhere, is there, that National Student Marketing Corporation might be having economic difficulties and is not able to carry on its business, is that correct? There isn't a hint of that.

A We never had a hint that that was in existence.

Q Didn't you know that $2 million of the 3.3 million

of unbilled accounts receivable booked through the first six months of '69, 2 million of them had been written off as no good and uncollectible?

A The Pontiac? The Pontiac contract had nothing to do with this. The company put the Pontiac contract on in February. They came to us and we said unless you have proper documentation, you must remove that Pontiac contract. We did not say that Pontiac contract was bad. We said we need more documentation because it was a small contract. They took it back out. That is as simple as that. You can't lump everything together like that.

Q You didn't give the reader of the proxy statement a hint that that had happened, did you?

A The Pontiac contract?

Q Yes, sir.

A There is nothing in the whole wide world that says we should.

Q All right. Is that your explanation?

A That is my explanation, yes, sir.

Q You see that chart, Chart No. 10 up there, also in evidence as Government Exhibit 17B and distributed to the jury. You have already told us this concerns itself with the footnote charged in Paragraph 3 of the indictment?

A Yes,sir.

Q You have prepared for your testimony, haven't you?

A Yes,sir.

Q You read the grand jury minutes?

A Yes,sir.

Q Did you review papers?

A Yes, sir.

Q Did you go over your testimony a few times before you testified here?

A I have read through it, yes,sir.

Q You have read through it?

A Yes, sir.

Q What you were going to say here in the last couple of days?

A I am sorry, I don't understand the question.

Q Did you go over the testimony that you were going to give to this jury before you came in here?

A Did I go over the testimony?

Q Yes.

A I went over a lot of the -- all these matters, yes,sir.

MR. STILLMAN: I would like you to please instruct the jury that that is a perfectly permissible,

indeed, a thing --

THE COURT: There is no debate about that.

MR. STILLMAN: Why the questions, your Honor?

THE COURT: Defense counsel asked similar questions

MR. STILLMAN: I didn't ask that question of any witness.

THE COURT: I didn't say that you did. I say generally in these cases defense counsel frequently ask them. There is no reason why Government counsel should not. You may be right. Maybe it isn't important. There is no reason it can't be asked.

Q On your direct examination, Mr.Scansaroli, you were asked twice, not once, but twice if you could recall discussing the changes in that very footnote with Mr. Natelli and you told this jury on your direct examination that you could recall no such conversation.

A I believe later on I said that there was nothing unusual for us to get together and discuss this type of situation.

Q After lunch, Mr.Scansaroli, you came back and told us something a little bit different.

My question to you,sir,is: You looked at your grand jury minutes over the lunch hour, is that right?

A Let me think a second.

Q Did somebody tell you what was in them?

A I am not sure.

Q Mr.Stillman showed it to you right here on the stand right after lunch, isn't that right?

A We looked at something in the grand jury minutes. I am not sure if it was that.

Q Did you forget what you had told the grand jury with respect to that footnote?

A I may have, yes,sir.

Q You have told us you don't recall any conversations about EasternAirlines or Pontiac at Pandick Press.

Do you want to change that testimony?

A No, sir.

Q You don't want to change that testimony.

Do you deny that there were such conversations?

A I can't recall any such conversations. Therefore I must deny them until I can see something that says it differently. I can't recall any conversation at the printer' office about those two contracts.

Q Do you deny your participation in such conversations?

A At the printer's office?

Q Yes, sir.

A I c-an't recall any.

Q You heard Mr. Buck describe the circumstances of that evening.

Did he have it right?

A As far as I can recall, yes, sir.

Q You heard Mr. Kurek describe the circumstances and what happened that evening.

Did he have it right?

A As far as I can recall, yes,sir.

Q In fact, Mr.Scansaroli, you thought that the fact that the Eastern Airlines contract had not been previously brought up was strange, didn't you?

A At that time, no, sir.

Q I am reading from your grand jury minutes of October 31, 1973, Page 77.

Question by Mr. McGuire:

"Q So it was determined by somebody that Eastern Airlines commitment was good, is that it?

"A Yes.

"Q What was the amount of that commitment?

"A According to that letter, $820,000.

"Q Did it occur to you that it was strange that a figure of that magnitude hadn't appeared on any of the reports that had been furnished to your accounting firm by the client until the eleventh hour?

"A Yes.

"Q Did you express that concern to anybody?

"A We did."

Did you forget that grand jury testimony?

A That doesn't say anything about the printer's office. Was that at the printer's office?

Q I asked you if you thought it was strange, sir, that the Eastern Airlines commitment wasn't mentioned?

A Yes, sir. If you asked me did we think it was stranger later on that this was not on the books as of May 31, yes, that is the problem we had. That is why we talked to somebody else in another office, as far as I can recall, because we thought it was strange.

Q You did think it was strange?

A Yes, sir. The letter was dated in May, but yet it was not on any schedules or on the books.

Q Let me just see if I understand you.

You thought it was strange later or at the time?

A We thought it was strange whenever it was brought to our attention brought to my attention. I don't believe it was at the printer's office.

Q You don't believe it was at the printer's office.

This is what you told to theSEC. I think you will find it is similar in spirit.

MR. STILLMAN: I am sorry, your Honor.

MR. VELIE: It is not offered as an inconsistent statement.

MR. STILLMAN: Similar in spirit testimony, it is a new one on me. I never heard that one before.

Q "Q Where were you when this decision was made to write it" -- meaning Pontiac -- "off? Were you in New York?

"A I don't think so. I don't know why I would be in New York if I was.

"Q Well, had the figures for this proxy statement been already assembled and is this in fact, this Pontiac commitment, written off in fact after the figures had been all gathered, do you know?

"A I don't know. A lot of times when you put the figures together they are preliminary and then you go back and change them.

"Q I notice there is another commitment, another fairly large one, Eastern Airlines. What were the circumstances with regard to that, putting that in the books?

"A I don't know."

You told us yesterday that those circumstances included a conversation of yours with Mr. Natelli and with Mr. Otkiss, is that correct?

A I recall a telephone conversationbetween Mr. Natelli and Mr. Otkiss.

Q Chart 65-15. Can you read it from where you are?

A Yes, sir.

Q Every single contract in this left-hand margin up to 10, a sub-total of $320,000, was still on the books, was it not, and includable as a portion of the earnings for the May period 1969, is that correct?

A I don't think I understand you. They were not -- it depends on whenever they were recorded. They were recorded some time after August '68. They would be part of the earnings of 1969.

Q They were still on the books, in any event, is that correct?

A The receivable as far as I know, yes, sir.

Q The company had as it wrote off contracts been deducting them from the current year sales, is that correct?

A Yes, sir.

Q All right. These were still on the books, is that correct?

A As far as I know, yes, sir.

Q In fact, were they not all acceptable for Tanya 1968 contracts? With I think three exceptions, these

were mostly contracts that were on your list when you first audited these contracts back there in October of 1968, is that correct?

A I will accept that,yes, sir.

Q Would you like to check it?

A No, sir.

Q Every last one of them had been brought to your attention either by yourself in your May SEC review or again by Mr. Oberlander or for the first time by Mr. Oberlander prior to the finalizing of that proxy, is that correct?

A We had comments I would say, yes, sir, on those contracts.

Q And the comments were by and large as reproduced here, these unfavorable comments, is that correct?

A I would say that is probably correct.

Q In addition, the Eastern Airlines contract, which I believe you told us was strange, it would come in at the eleventh hour, $519,000 was a component of the May 1969 portion of the proxy statement, is that correct?

A It was strange from the standpoint that it was not already on the books at that point because it was dated in May. Normally if a contract is dated as of May, it would be recorded as of the end of May.

Q It wasn't so unusual for National Student Marketing, was it?

A It was unusual in this sense, yes.

Q The Pontiac commitment was recorded as of February, after the period in April, isn't that correct?

A Yes, sir, but that was an internal situation.

Q All the 1968 contracts came up in October and the ones that were dated were dated in October and you included those in the period that had been in August, is that correct?

A Yes,sir. They were commitments as of August.

Q In any event, a total of such contracts on the books of over $830,000, almost $840,000 of these contracts is that correct?

A That is a selected list from all the contracts as of that date.

Q We have selected he ones which are, (A), still on the books, (B), brought to your attention either personally or by Mr. Oberlander and, (C), have comments of this kind on them?

A Yes, I agree with that.

End 7AM

Q A total of $840,000 of such contracts, is that correct?

A That list, yes, sir.

Q Did it occur to you in August of 1969 as you did your SEC review that after all you learned about unbilled accounts receivable accounting at National Student Marketing that it might be just a little bit chancey to allow this much to stay on the books without some warning to people who were going to read that public document?

A No,sir. You got to understand that, first of all, the first review I made was in May. When the company decided not to prepare the proxy statement as of that date we bound those papers up and as far as I know we never went back to look at them. So our main concern as of the end of May, for the May figures, Mr. Oberlander made his review in August, was to ascertain whether the receivables on the books were correct as of that date.

Mr. Oberlander made his review and prepared his work paper and that is what we were mainly concerned with. We did not have charts like this to look at everything in order.

Not only that, there weren't that many things like you were talking about. You talk about the Pontiac

contract, which we had nothing to do with, and the Ron Michaels contracts was an unusual situation because of the employee. Those are two major items you are talking about and they are just unusual items that would not lead you to the conclusion that you are saying that we should arrive at.

Q Mr.Scansaroli, Government Exhibit 25 is the final proxy. There is in here a description of the company, National Student Marketing, Pages 15 and 16. It reflects that sales of services in 1968 --

MR. MARTIN: Can we have the page?

MR. VELIE: Page 16.

MR. MARTIN: 16?

MR. VELIE: Yes.

MR. MARTIN: Just one minute, please.

Q It indicates, doesn't it, to anybody who read the description of the business of this company, that the most profitable item of its sales of services are fixed fee contracts? Isn't that what it says?

A "Their percentage of total produce revenues was 30 per cent, 25 per cent and 45 per cent, respectively. Sales of services in 1968, listed by category and in order of profitability, were as follows: Fix fee contracts,

foreign study programs and prepared sales programs."

Q It is fair to say that in order of profitabiltiy fixed fee contracts come first according to the proxy statement, is that right?

A Per that proxy statement, yes, sir, but we had nothing to do with those statements. It depends on how you look at it.

Q That wasn't true, was it?

A I don't know if itis t[illegible] or not.

Q But you do know --

A No, I don't.

Q -- those fixed fee contracts were written off?

A But the thing is you are talking about profitability, which is more profitable. You have three different types of work that these people do and you have a lot of other expenses. If you take into consideration all the other expenses which is more profitable? I don't know. Those comments were not written by the auditors. They were written by company personnel.

Q A reader who had the true economic facts would be able to see through that nonsense, wouldn't he?

MR. STILLMAN: I object to that.

A I don't understand the question, sir.

Q Mr.Scansaroli, you were aware, weren't you,

that National Discount Marketing through its officers periodically would issue predictions of what it would earn during the year?

A I became aware of that some time I believe in the summer of '69, maybe early 1970.

Q The figures frequently used were figures calculated as earnings per share, is that correct?

A Yes,sir.

Q That means simply you take the total number of the shares, the total amount of the earnings, you do an arithmetic computation and come up with the amount of earnings that there is per each share, is that correct?

A Yes,sir.

Q The company had predicted that it wanted to meet certain earnings per share goals during the year, is that the idea?

A I believe -- you know, Mr. Randall would usually make these comments to meetings that he used to attend. I had nothing to do with that.

Q Look at this page on Exhibit 53 for identification and tell me if that is your handwriting.

A Yes,sir.

y Mr.Scansaroli, was it any secret to you that in addition to writing on these sales and then replacing

them with new sales what the company was doing was writing on the sales or writing them off and adding the new companies, adding together their pooled earnings? You knew that they were doing that,didn't you?

A I am not so sure I can answer that type of question. You are saying they are adding them on, pulling them off. I don't understand the question.

Q As the company wrote off these uncollectible sales it was also at the same time acquiring new businesses, wasn't it?

A Yes, sir.

Q It was acquiring them under an accounting method which permitted them to pool or add in the earnings of those companies as if they had always been earned, is that right?

A Some companies, yes,sir. Some companies were purchased.

Q The effect of this was if earnings of National Student Marketing were written off and a new company was pooled in,that new company could in a sense replace the earnings which were being written off, is that correct?

A I wouldn't say that, no.

Q You wouldn't say that. Did you prepare various schedules showing the acquisitions needed to be made in order

that the earnings projections would come out all right?

A At what point in time?

Q After you went to work for National Student Marketing, sir.

A Yes,sir, I think I did.

Q In fact, you jumped right into the spirt of things, didn't you?

MR. STILLMAN: I object to that, your Honor.

THE COURT: Sustained as to form.

Q Mr.Scansaroli, let's just look at this together for a minute,Exhibit 53. The first page on here is an audit status sheet as of October 10, 1969. It shows, does it not, the components of the consolidated company as of that date, is that correct?

A Yes, sir.

Q National Student Marketing's contribution to the family of companies was a $1.5 million loss? Is that correct?

A Yes, sir.

Q There is a whole long list of subsidiaries here which were later acquired and changed that loss into a gain of about $2 million, is that right?

Do I have that right? Is that $2.7 million? I will take your word for it.

A I believe -- it doesn't say so, but I believe they round it off or the series are left off. So that could be 2.7 million.

Q Further in the schedule, at a little later time -- this is November 20 -- National Student Marketing's loss is larger, isn't it, $1.7 million, is that correct?

A Yes, but I don't know at what point this was.

Q It bears the date of October 10.

A But they don't close their books at October 10. This was prepared, I believe, around that point in time, but this doesn't say for what period.

Q There is no point in arguing about it. This appears to be a later paper, doesn't it, the second one?

A I don't know if it is a later paper. I can't tell.

Q It is dated November 20, isn't it?

A Yes,sir.

Q It is in your handwriting?

A Yes, sir.

Q It has got a loss for National Student Marketing of $1.7 million?

A Yes, sir.

Q And it has a few more acquisitionees or new companies added at the bottom, doesn't it? For instance,

it adds Interstate, is that correct?

A Interstate --

Q I am sorry. Interstate is on here.

A I think it is the same companies.

Q Okay. A larger loss, an additional schedule with a similar loss for National Student Marketing.

Here is one which apparently does not bear a date, again, in your handwriting, is that correct?

A Yes, sir.

Q Here NationalStudent Marketing's loss is over $2 million, is that right?

A Yes, sir.

Q This time there are new subsidiaries being accounted for on this sheet, isn't that right?

MR. STILLMAN: What is the period of time we are now talking about?

Q Can you tell us?

A The paper is dated for the period ending 8/31/69.

MR. STILLMAN; Is this a document prepared after Mr. Scansaroli goes to work for the ocmpany?

MR. VELIE: Yes.

MR. STILLMAN: I will object to the relevance of this, your Honor.

MR. MARTIN: I move to strike it, your Honor.

THE COURT: Overruled.

Q Adds some new subsidiaries, Simmons, Varsity House, Stuckey & Speer. You know what that is? That must be Educational Services.

A Yes. I don't know if they acquired these companies at this point though.

Q That is correct. Some of these have not been acquired yet, is that correct?

A I don't know.

Q But the calculation you are making on this page is what their contributions would be to earnings per share, is that correct?

A Yes,sir.

Q In fact, this little group of Simmons, Varsity House,Educational Services and S & S change 53 cents per share to a larger figure of 72 cents per share. Do I have that right?

A As of that date, yes, sir.

Q You call these pro forma adjustments or some of these other things are pro forma adjustments, is that right?

A We were trying to come up with an estimated figure at some point in time.

Q Here is another calculation in which you are working on earnings per share. You indicate that if you sold two losing subsidiaries, Cal and Compujob, that is an improvement in your earnings per share by 8 cents, is that correct?

A Yes, sir.

Q So by this page you could get your earnings per share by that process up to 74 cents per share, is that right?

A Well, making all these adjustments, selling these two companies and acquiring these companies, it would end up with 74 cents a share.

Q You wrote this note, didn't you?

A Yes, sir.

Q The note says "Bernie, suggest you buy that shirt company as soon as possible"?

A Yes, sir. That was part of my job. My job was preparing financial statements for the company, preparing earnings per share, and so forth.

That is why they hired me. I put the figure together for them.

MR. STILLMAN: Finished, Mr. Velie?

MR. VELIE: Yes.

REDIRECT EXAMINATION

BY MR. STILLMAN:

Q Who asked you to prepare those schedules?

A Mr. Kurek.

Q Was he the man that you worked for in National Student Marketing Corporation?

A Yes, sir.

Q Mr.Kurek with the $500,000 worth of options, right?

A Yes,sir.

MR. VELIE: Your Honor, I object to that.

THE COURT: Yes. I don't think that has anything to do with redirect at all.

Q I show you this memorandum. Will you tell me whether or not it is prepared by you at or about the date it bears.

A Yes,sir.

MR. STILLMAN: Can we mark this as the next Scansaroli exhibit.

xx (Defendant SCansaroli Exhibit P was marked for identification.)

MR. STILLMAN: I offer it, your Honor.

MR. VELIE: No objection.

xxx (DefendantScansaroli Exhibit P. was

received in evidence.)

MR. STILLMAN: May I read it to the jury, your Honor?

THE COURT: Surely.

MR. STILLMAN: This is a memorandum, ladies and gentlemen, dated January 12, 1970, from Joseph Scansaroli to Bernie Kurek, and John Stalick.

(Mr. Stillman read from Defendant Scansaroli Exhibit P in evidence to the jury.)

THE COURT: We will break now for lunch, ladies and gentlemen, and resume at 2:15.

(Luncheon recess.)

AFTERNOON SESSION

2:15 p.m.

xx JOSEPH SCANSAROLI, resumed.

(In open court, jury present.)

THE COURT: Yes, sir.

xx CONTINUED REDIRECT EXAMINATION

BY MR. STILLMAN:

Q Mr. Scansaroli, Exhibit P which we read to the jury this morning is a memorandum which you sent to Mr. Kurek and Mr. John Stalick, is that right?

A Yes, sir.

Q And Mr. Kurek was the chief financial officer of the company, is that right?

A Yes, sir.

Q Who was John Stalick?

A He was the controller.

Q In the scheme of things, is the chief financial officer and then John Stalick, the controller, was he the second in command in the Financial Department of that company?

A Yes, sir.

Q What was your job title?

A I was assistant controller.

Q In other words, you answered to Stalick and you

also answered to Kurek, is that correct?

A Yes, sir.

Q Mr. Velie asked you about some events at the printer on August the 14th and he referred you to some testimony of Mr.Buck and Mr. Kurek with respect to conversations about Eastern and/or Pontiac.

Do you recall whether or not either of those men testified that you said anything about those subjects during the course of that evening at the printer?

MR. VELIE: Objection to what he recalls other people testifying.

THE COURT: The jury performs that function, not Mr. Scansaroli.

MR. STILLMAN: Yes, sir.

Q Mr. Velie showed you this chart, 65-15.

A Yes, sir.

Q Was one of the items on the schedule which Mr. Oberlander gave to you Syntex?

A Yes, sir.

Q And that was a commitment of over $120,000 which you insisted be written off, isn't that right?

A Yes, sir.

Q That was the largest single commitment among any of those discussed on those charts, isn't that correct?

A Yes.

MR. VELIE: Excuse me, your Honor, this is redirect, but he's putting words in the witness' mouth. I don't think that's necessary.

Objection to leading.

THE COURT: We will let it stand. I will ask Mr. Stillman not to lead.

If memory serves me, there's another problem here though. We covered this on direct. I don't know why we have to repeat it.

MR. STILLMAN: There was just that question, your Honor, and I'm moving on to something else.

Q Mr. Velie asked you about whether or not you prepared for your testimony in this trial.

do you recall that?

A Yes, sir.

Q He asked you whether you reviewed documents.

Do you recall that?

A Yes, sir.

Q In the course of your preparation for testifying here, did you have any conversation with me with respect to whether or not you had to testify?

A Yes, sir.

Q What did I tell you on that subject?

MR. VELIE: I object to what Mr. Stillman told him, your Honor.

MR. STILLMAN: It is his statement of mind, your Honor.

THE COURT: I'm sorry. I don't accept that. To make absolutely sure, I'll get it read back. I don't accept that.

Could we have it read back.

(Question read.)

THE COURT: I must say I don't really understand the question. I certainly think generally speaking the objection is well founded. I don't think it is proper to go into your internal conversations preparing for trial.

Q Did you have any understanding, sir, with respect to whether or not you could or could not testify at this trial?

A Yes, sir.

Q What was your understanding, sir?

A My understanding, I did not have to testify.

Q Mr. Velie asked you about a matter, some matters in the grand jury, some matters before the Securities and Exchange Commission.

Do you recall that?

A Yes, sir.

Q As to a particular piece of testimony, he asked you whether you forgot something you had said on one of those two bodies.

Do you recall that?

A Yes, sir.

Q How many times did you testify before the SEC?

A I believe it was three times.

Q How many times before the grand jury?

A One time.

Q Looking at this looseleaf, is that your testimony before those two bodies?

A Yes, sir.

Q Was there any lawyer sitting alongside of you who could make objections to any of the questions that were put?

MR. VELIE: Objection. This has not only been proved before --

THE COURT: We have gone into that. It is established that he went without a lawyer. We don't have to repeat that.

Q Mr. Velie asked you some questions with respect to the commitments and the work that you did in connection with the August 31, 1968 audit.

In the course of your work on that audit, did you

speak to Bernard Kurek?

A Yes, sir.

Q About the commitments?

A Yes, sir.

Q Did you speak to Cortes W. Randall about the commitments?

A Yes, sir.

Q Did you speak to Ron Michaels about the commitments?

A Yes, sir.

Q Did you speak to other account executives about the commitments?

A Yes, sir.

Q Did you believe that any of those men were lying to you?

A No, sir.

Q Did there come a time, Mr. Scansaroli, with respect to the May 31, 1969 statements that a representation letter was prepared by Mr. Kurek or signed by Mr. Kurek with respect to the state of affairs on the May 31, 1969 financial statements?

A Yes, sir.

Q I show you Government's Exhibit 24, page 2154, and ask you if that's the letter? (Handing).

A Yes, sir.

Q At the time that that letter was signed, was John Stalick the controller of National Student Marketing Corporation?

A Yes, sir.

Q Did you have any reason to believe that John Stalick would lie to you about anything?

A No, sir.

MR. VELIE: Excuse me. I object to the form of that question, your Honor, as it tends to suggest somebody is lying.

THE COURT: Sustained.

MR. STILLMAN: May I read Government's Exhibit 24, page 2154, to the jury, your Honor?

THE COURT: Yes.

MR. STILLMAN: Thank you.

(Mr. Stillman read from Government's Exhibit 24 in evidence to the jury.)

Q Finally, Mr. Scansaroli, with respect to the job offer, what is your best recollection, sir, of when for the first time you had any conversation with anyone at National Student Marketing Corporation concerning the possibility of your coming to work for that company?

A Either late spring or sometime during the summer of 1969.

Q Do you recall who it was who approached you on that subject?

A I was approached on several occasions by both John Stalick and Bernie Kurek.

Q What did you say to them at that time?

A I indicated I wasn't interested.

Q Did you have a responsible position at Peat, Marwick, Mitchell at that time?

A Yes, sir.

Q As of that point in time what did you see as your future at Peat, Marwick, Mitchell?

A I thought I had a good future.

Q What was the next step up the line for you at Peat, Marwick, Mitchell?

A Manager.

Q After manager?

A Partner.

Q Did you believe at that time that you had the opportunity to achieve that kind of success?

A Yes, sir.

Q In any of thework that you did after the time that you had these conversations and, of course, indeed, before, but I am talking about this job offer, did that fact play any part at all in the work that you did for this company?

A No, sir.

Q Did you do anything, did you make any decision or do anything as a result of that offer which did not represent anything but the best efforts you could to do a job for this company?

A No, sir.

MR. STILLMAN: I have nothing further, your Honor. Thank you.

THE COURT: All right, Mr. Scansaroli, you may step down.

MR. VELIE: Your Honor, I just have one very brief question.

xx RECROSS EXAMINATION

BY MR. VELIE:

Q The memorandum Mr. Stillman read to you, Mr. Scansaroli, Exhibit P, you wrote that on January 12, 1970,

is that correct?

A Yes, sir.

Q That was shortly after the SEC began its investigation, wasn't it?

A I am not sure.

Q Why don't you just take a look at this and see if that refreshes your recollection. Does that help you fix the date?

A This is a letter sent to --

Q Sent to the SEC, isn't it?

A Well, it is addressed to White and Case.

MR. VELIE: Perhaps we should have this marked just so the record reflects what we are talking about. Government's Exhibit 66 for identification, please.

xx (Government's Exhibit 66 marked for identification.)

Q Mr. Scansaroli, I am just going to ask you to read it to yourself for now and see if the material in here indicates to you the date at which the company started responding to SEC inquiries?

A On January 5, 1970.

Q January 5?

A Yes.

Q That is seven days prior to Exhibit P, the memo you

wrote?

A Yes, sir.

MR. VELIE: I have nothing further.

MR. STILLMAN: Can I see that?

MR. VELIE: Sure.

MR. STILLMAN: Can we identify this for the record, at least, as to what the document is?

MR. VELIE: If the witness knows it.

MR. STILLMAN: Let's you and I do that.

I would just like the record to indicate what the witness was shown, your Honor.

THE COURT: It can or cannot be. I don't know what the point of this is. Just because a document is marked doesn't mean it has to be delineated on the record as such.

MR. VELIE: I have no objection, your Honor.

THE COURT: If you have no objection, fine.

Q Have you seen this before?

A I am not sure.

MR. VELIE: In any event, there is no dispute, I think, that it is a National Student Marketing letter to its lawyers regarding a request made by the SEC for information.

MR. STILLMAN: Signed by whom?

MR. VELIE: THis particular letter is signed by Mr. Kurek.

MR. STILLMAN: Thank you, sir.

MR. VELIE: Surely.

MR. STILLMAN: Mr. Scansaroli.

(Witness excused.)

MR. MARTIN: Call Leon Otkiss.

xx L E O N P. O T K I S S, called as a witness by the defendant Natelli, having been first duly sworn by the Clerk of the Court, testified as follows:

MR. MARTIN: Your Honor, I believe this brings us to a matter which your Honor said you would take up outside the presence of the jury before we proceed.

THE COURT: I have no doubt you are correct, but I am frank to say I don't know what you are talking about.

MR. MARTIN: This has to do with a pretrial motion that we made that you said was without prejudice to our right to renew. We brought it up at the trial.

THE COURT: I am sure you did, but there have been so many motions I don't know which you are talking about. I don't mean to be critical. I am just observing that I honestly don't know what you are talking about.

MR. MARTIN: Can we come up to the side bar?

THE COURT: Surely.

(At the side bar.)

MR. MARTIN: Your Honor, Mr. Otkiss is one of the

people who filed affidavits in support of the motion to get discovery of his grand jury testimony prior to the time he testified to allow him to refresh his recollection as to the events at issue as the Government refreshes his recollection of its witnesses before they testify. That was the motion we made prior to trial.

THE COURT: I am sure you did. I have heard of Otkiss in other contexts during the trial. I apologize, but I don't recall all the many motions that were made in this case and this application at the moment. I suppose I should have total recall, but I don't. Now that you refresh me I understand.

Did you hear that, Mr. Velie?

MR. VELIE: Yes, your Honor, and I heartily object. This witness is a partner in the firm of Peat, Marwick and Mitchell. He is very much interested in the outcome. His testimony before the grand jury may limit what he will be able tnowto volunteer to help his good friend Tony Natelli and I believe we should be permitted to cross examine him the way we would cross examine any other witness who appeared before the grand jury.

THE COURT: I am inclined to agree that you are right, even assuming he is not with Peat, Marwick, Mitchell. I don't see any reason to turn over the records to him or to

allow him the comfort of that at all. But I will reserve final decision until I hear what it is all about.

I assume the only relevant evidence he can give would be a very narrow compass, namely, his conversations and actions with respect of the comfort letter.

MR. MARTIN: Yes, your Honor, and his work on the proxy. The only thrust of our motion is that it is unfair to allow the Government to have a grand jury proceeding and then use the transcripts of that proceeding to refresh the recollection of its witnesses before they testify and are cross examined and at the same time to deny to the defendant the right to use the same type of evidence to refresh the recollection of its witnesses before they testify.

THE COURT: You may say that is unfair, but it has been done for him, many years. I don't quite get as excited about it as you seem to. I am sorry.

MR. MARTIN: I would hope we could move the law forward.

THE COURT: Perhaps. As I see, I am going to listen to what this is all about before I get interested in ruling finally because I don't even have the slightest notion that he even testified on these subjects before the grand jury. I wouldn't know. I would be the last to know. Nobody has ever shown me his minutes.

MR. MARTIN: He has filed an affidavit to that effect with the Court, your Honor.

THE COURT: His affidavit, whatever it said, didn't get down to the particulars of what I now know much better than he knows as to what has happened at this trial. This is a futile discussion.

Please. You know what I am trying to say. I have no idea what you are going to ask him and I am not about to embarrass you by asking. Do the same for me. Let's go forward.

(In open court.)

DIRECT EXAMINATION

BY MR. MARTIN:

Q Mr. Otkiss, what is your present occupation, sir?

A I am a partner in the firm of Peat, Marwick, Mitchell and Company. I am a certified public accountant.

Q Are you a partner of Tony Natelli?

A Yes, I am.

Q In what office do you presently serve, sir?

A In the Washington, D. C. office.

Q That is the same office that Mr. Natelli presently serves in, is that correct?

A That's correct.

Q Mr. Ottkiss, directing your attention, sir, to the

year 1969, where were you working at that time?

A I was a partner in the Philadelphia office of the firm.

Q Did you have any responsibilities in 1969 other than that of a regular partner in the firm of Peat, Marwick, Mitchell in the Philadelphia office?

A I was one of our firm's SEC reviewing partners.

Q Would you tell the ladies and gentlemen of the jury what it meant to be one of the firm's SEC reviewing partners?

A Well, our group of SEC reviewing partners were a group of technical partners in the firm whose responsibility under our firm policy was to review all or certain types of filings with the SEC, primarily proxy statements, registration statements.

We also reviewed other offerings of securities, those filings, whether they were with the SEC or other regulatory agencies.

Q Mr. Otkiss, you have some of my problems. You speak quickly and sometimes not as loudly as you should. Would you try and speak up, speak slowly.

You say, sir, that the SEC reviewing partners were technical partners. What do you mean by that phrase, sir?

A Well, they were probably the most technical proficient partners in the firm. They were the more

experienced partners. They had a lot of experience with public filings, things of that nature.

Q When you say technically proficient, do you mean in terms of the application of various accounting rules and regulations?

A That's correct.

Q Directing your attention specifically to August of 1969, did you have occasion to do any work in connection with a proxy that was being prepared for a merger between National Student Marketing Corporation and the Interstate Insurance Company?

A Yes, I did.

Q In August of 1969 how old were you, sir?

A About 47.

Q Do you know how old Tony Natelli was at that time?

A Inhis early thirties, I believe.

Q What was your assignment with regard to the proxy that was being prepared for National Student Marketing Corporation at that time?

A The New York office would assign his SEC reviewing partners to the various engagements and I was assigned to review the proxy statement that was to be filed.

MR. MARTIN: Could I have Government Exhibits 5, 17, 17A and 25, Mr.Velie? 17 also, sir.

(Pause.)

Q As the SEC reviewing partner assigned to work on this proxy,what information, sir, would be made available for you?

A Well, the standard practice I would get copies of all proofs that were prepared in connection with the filing and my usual practice would be to askfor copies of either annual reports or for 10K in which the firms report and on the financial statements.

I would use those, readingthose when I read the proxy material.

Q Iwant to put before you, sir, a draft of the

proxy statement we marked in evidence as Government Exhibit 17A. Would you just look through that and tell us whether you during that period had occasion to review such a draft?

A Yes. I don't know if it was this draft, but I did review a draft of the proxy statement,yes.

Q I show you Government Exhibit 17 and ask you to look through that and tell us whether you had occasion to review a copy of that same draft?

A Well, again I don't know if it was the same draft, but a draft of this filing, yes.

Q I want to put before you, Mr. Otkiss, Government Exhibit 17B, which has been identified as basically a portion of the same footnote that appeared in the draft of August 9, 1969, a proof that has been identified in the center as having Mr. Natelli's handwriting on it and the final portion of the proxy as it was published and filed.

In your work onthe proxy did you have occasion to have any conversation with Mr. Natelli about the method of accounting that the company was using to record income on contracts in progress?

A Yes, I did.

Q Would you tell the ladies and gentlemen of the jury as best you can recall -- first, was that a conversation that took place in person?

A No, it was by telephone.

Q Who were the parties to that telephone conversation?

A Mr. Natelli and myself.

Q Can you recall for us as best you can the substanc of that conversation, what you said to Mr. Natelli and what he said to you?

MR. VELIE: Just the date, Mr. Martin.

Q And ~~(A?)~~, can you fix the date of this conversation?

A It was some time in early August, but I can't be specific about the date.

Q Now, can you tell us the substance of the conversation?

A Well, if I can expand on the procedures that I would normally follow in reviewing the material. I would normally get the proofs. I would read through them, look to the annual reports of the 10K's to see whether they were in agreement. Normally I would go through the proof and make a number of questions in the margin and after I completed --

MR. VELIE: Excuse me, my objection is that the answer is not responsive. He was asked what Mr. Natelli and he were talking about.

THE COURT: I agree, Mr. Martin, unless you

want to change your question.

MR. MARTIN: I will be happy to change the question.

Q I ask you, sir, to continue, if you would, telling us what you would do when you were first getting into a proxy situation.

THE COURT: Haven't we already had this? We have the standard practice. Isn't that repetition?

MR. MARTIN: He was just giving the context of this particular conversation, what he had done before that.

Let me do it another way.

Q Prior to the time that you talked to Mr. Natelli about this, had you had occasion to review any material?

A Yes.

Q What was the material that you had reviewed?

A The proofs of the proxy statement and I would have read either the annual report or the Form 10K, whichever I happened to have.

Q Do you recall, sir, whether you had any conversation with Mr. Natelli about the method of accounting that the company, National Student Marketing, was employing on the contracts in process?

A Yes. This was one of the questions I raised

upon review of the proxy material.

Q Would you, as best you can recall, tell the ladies and gentlemen of the jury what that conversation was, what you said to Mr. Natelli and what he said to you?

A Well, my basic recollection is when I first read the note with respect to the method of income recognition, I had some question about it, it seemed somewhat unusual. I spoke to Mr. Natelli about it. He gave me the basis for which the company was recognizing income.

He indicated that it was an attempt to match effort with revenues and income and earnings, and after discussing it with him it seemed to be an appropriate method.

Q Was there any question as to whether or not the commitments that the client was using were oral or in writing?

A Mr. Natelli told me that as of August 31, 1968, the commitments had been oral commitments, but subsequently he was insisting that they be in writing. So the commitments with respect to the period subsequent to August 31, 1968, were to be in writing.

Q Did you say anything as to your reaction to the use of oral commitments and the change to written commitments?

A I was much happier to see the commitments being

in writing, although an oral commitment of itself wouldn't of itself be wrong.

I was still more satisfied to see them in writing.

Q If you had disagreed, sir, with the method of accounting being used in the proxy statement, what would be the procedure for you to follow in the firm?

A Initially I would talk to the engagement partner, who in this case was Mr. Natelli, and if the disagreement continued I would take it to our professional practice department.

Q Did you take this question to the professional practice department?

A No, I did not.

Q Directing your attention, sir, to Government Exhibit 17B, which is the trip ticket. So the juryc an follow us, a chart --

THE COURT: Do you want to move that a little closer?

(Pause.)

Q You note, sir, on that exhibit there are changes made with regard to a footnote that appeared in the original draft of proxy.

A Yes.

Q Did you have occasion to have any conversation with Mr. Natelli about the changes that were made in that footnote?

A Yes, I did.

Q Would you tell the ladies and gentlemen of the jury, was this a conversation that was in person or face to face or was it on the telephone?

A This was a telephone conversation again.

Q Who were the participants in that telephone conversation?

A Mr. Natelli and myself.

Q When did this take place?

A Again, some time in early August.

Q Now would you tell us, sir, as best you can recall the conversation, what you said to Mr. Natelli and what he said to you?

A Well, I can't specifically recall how the question was first arrived,but we discussed the need for a footnote and he told me that it related to the fact that there were a number of commitments that were found to be I guess fraudulent. There had been an employee working for the company who had booked certain commitments that didn't exist.

Q Was there any discussion of the magnitude of these

commitments?

A Yes. They were something in the magnitude, five,six, $700,000.

Q What else was said on the subject?

A We also discussed at that time another adjustment that related to deferred taxes. I think possibly I may have felt that the note as originally drafted wasn't that clear or wasn't informative, maybe didn't make sense. I am not sure. But we discussed the substance of it. We discussed it in the light of the fact that the financial statements had to be restructured because companies had been pooled subsequent to August 31, 1968, additional companies had been acquired.

So that the financial statements were going to be restated.

In going over all the factors, the magnitude of the effect on net income, the offsetting effect of the deferred taxes on net income, we concluded or he told me and then I agreed with him that it was about a twenty-odd thousand dollar effect on net income, and we didn't consider that to be material.

Q Was there any discussion as to whether or not as a result of that fact there should or should not be a disclosure of the fact that these writeoffs had taken place?

A We discussed this at the time. Mr. Natelli told me that it was difficult, in effect, to write a footnote, to make any sense out of it because of the nature of it, the fact that this man had fraudulently booked these contracts. It just didn't seem to have that much significance.

Q Was there any discussion about any changes of procedure that had taken place in the intervening year?

A Well, again we did discuss the fact that commitments were to be in writing and hopefully that would eliminate this situation from occurring again.

Q What was the conclusion that you and Mr. Natelli reached with regard to the question of whether or not there should be disclosure of these items?

A We concluded that it did not have to be disclosed, again because it had no material impact on net earnings.

Q Did you, sir, as the SEC reviewing partner assigned by Peat, Marwick to this matter, suggest to Mr. Natelli at that time that APB 9 required disclosure of these types of adjustments?

A I don't recall that I even focused on APB 9 at that time. I just have no recollection of it.

Q You will note, sir, that in the third part of this exhibit, which is the proxy as it finally appeared, the figure for the sales originally reported did not change but the figure changed as to the pooled companies reflected retroactively.

Can you recall now, sir, whether you were aware of that fact at the time?

A I don't recollect specifically that I was aware of it. I probably was, but I don't have a recollection of it.

Q Do you recall, sir, whether or not you ever suggested to Mr. Natelli that it would be wrong to reflect that an adjustment in the pooled companies line?

A No, I don't recollect a conversation of that nature at all.

Q Let me put before you Government's Exhibit 19. Government's Exhibit ~~18~~ 19, so the jury is familiar with what we are talking about, is a document in evidence. It is a letter dated August 14, 1969, signed by Thomas E. Mullen, on the letterhead of Eastern Airlines.

Mr. Otkiss, can you tell us, do you recall whether or not you had occasion in August of 1969 to discuss with Mr. Natelli the question of booking a commitment for Eastern Airlines?

A We may have, but I have no recollection of it.

Q Looking at that letter, sir, is there anything in that letter that would cause you to conclude that the company could not book revenues as of May 31, 1969 on the basis of that letter?

MR. VELIE: Excuse me. I am going to object to that. He didn't apparently talk to Mr. Natelli about it. It is irrelevant what he now thinks.

THE COURT: Yes, and for another reason which I just as soon not reveal at this moment, I think that's a sound objection.

Q I show you Defendant Natelli Exhibit K and ask you, sir, what is that document. Have you seen it before?

A Yes, I have seen a copy.

Q A copy of that?

A Yes.

Q Did you see a copy of that during the fall of 1969?

A I would say yes, after it had been issued.

Q That document has already been identified. Will you tell the ladies and gentlemen of the jury what it is.

A This is a letter addressed to National Student Marketing Corporation and Interstate National Corporation from our firm which was required to be written in connection

with the merger agreement. The merger agreement required the firm issue what we call a comfort letter and it was provided for in the terms of the agreement.

Q Mr. Otkiss, did you have occasion to have any discussions with anybody concerning that comfort letter in October of 1969?

A Yes, prior to its issuance.

Q Would you tell us what your first contact with that comfort letter was?

A On the morning of October 31, I believe, I received a call from a Mr. William Colona, who was a manager or supervisor in the Washington office at that time, telling me that it was the day to issue the comfort letter but that we would not be able to issue it in the form required by the agreement because apparently during the course of work he was then doing there were certain adjustments that affected the May 31, 1969 unaudited financial statements.

I told Mr. Colona at that time to speak with Mr. Natelli and have him call me back so that we could discuss this matter.

Q Did you subsequently speak to Mr. Natelli?

A Yes, I spoke to Mr. --

Q Again, before you tell us about that conversation, Mr. Otkiss, if you would try to speak up and a little

more slowly.

Would you tell us what your conversation was with Mr. Natelli. Approximately when did it occur?

A It occurred sometime later in the morning on October 31. We discussed the nature of the adjustments, the fact that apparently the May 31 unaudited financial statements showed a profit -- and I am not sure that I recall the exact figure -- something of seven or $800,000 magnitude, and that as a result of these adjustments there was little or no earnings during that period.

I asked him at the time or we discussed at the time whether or not management had been informed of what our concerns were. I don't recall at that time whether he had spoken to anyone in management. I also asked him to find out what management intended to do about it.

We also arranged to have a call with one of our partners in New York in the Department of Professional Practice to discuss this matter and see what had to be done.

Q Who was the partner in New York that you were going to set up a call with?

A Mr. Thomas Holton.

Q What was Mr. Holton's association with Peat, Marwick at the time?

A Mr. Holton was a partner. He was in our depart-

ment of Professional Practice. He was what I would call our top SEC reviewing partner.

Q Did you have such a conversation or conference call with Mr. Holton and Mr. Natelli?

A We had a conference call, again, that same morning, sometime around lunch time, and basically it was for the purpose of informing Mr. Holton of what the problems were and to get some direction as to what action had to be taken.

Q Subsequent to that call with Mr. Holton, did you have any further contact with this comfort letter on that day?

A On that day, toward the end of the day, I received a call from Mr. Natelli and he told me at that time that although the letter did not comply with the requirement of the merger agreement that apparently the merger had gone ahead.

Q Was there any discussion about what Peat, Marwick was planning to do at this point?

A My best recollection is that people in New York were going to discuss this and see what action should be taken. I don't have any precise recollection of specifics.

Q Did you ultimately learn what action Peat, Marwick's people in New York had decided to take?

A Yes. On Saturday evening, at home, the following Saturday, Mr. Holton called me to tell me that they had

discussed this matter in the department, apparently had discussed it with our firm's legal counsel, and that as a result thereof they decided to send copies of the comfort letter to all members of the board of directors of both companies.

Q Who was the firm's legal counsel to whom Mr. Molton referred?

A Mr. Victor Earle.

Q Mr. Otkiss, in any of his conversations with you on that day, the conference call, at any other time when this comfort letter was under consideration, did Mr. Natelli ever say anything to you or suggest to you anything that would indicate that if this thing came to light Mr. Natelli would have some personal problems?

A No, he did not.

Q Did Mr. Natelli ever tell you that he had to cover up what went on at NSMC?

A No, he did not.

MR. MARTIN: I have no further questions, your Honor.

THE COURT: Ladies and gentlemen of the jury, we will take an afternoon recess at this point.

Counsel please remain.

(Jury left the courtroom.)

THE COURT: Mr. John Martin, I just want to tell you that I, as you saw, perhaps, did borrow a copy of the grand jury minutes of Mr. Otkiss, read them, and I have listened to what he said, and I see no reason to change the ruling.

I think there are rather simple but sound policy reasons why it would be just as well if we left things stand with the traditional view, which I understand to be that the witness doesn't get a chance to read his grand jury minutes. If I had thought otherwise at this point I would interrupt, before Mr.Velie had his chance to cross examine, and take time out to let Mr. Otkiss review his minutes, which are relatively brief, simple, general, and wouldn't take very long. But I think Mr. Velie is right and I think, frankly, the interest of truth and justice would be much better served if we adhere to what I understand to be the traditional view.

Exception to you and your client.

MR. MARTIN: Thank you, your Honor.

MR. STILLMAN: Your Honor, if he chooses to cross examine with respect to anything in there, I assume at that point we would have an opportunity to review the document.

THE COURT: At that point, in view of what I see in the minutes, I would think there would be no undue upset

to the United States Government if that were permitted. I am not sure there is any rule of law that supports that, but I see no objection to it, unless Mr. Velie does.

MR. VELIE: No, your Honor.

THE COURT: The minutes are, as I said, really quite brief. Frankly, they don't go into even as much as Mr. Martin's direct brief examination did.

MR. MARTIN: And loud, Judge.

(Recess.)

(In open court, jury present.)

THE COURT: Mr. Stillman, do you have any questions of Mr. Otkiss?

MR. STILLMAN: No, sir.

MR. VELIE: May I proceed, your Honor?

THE COURT: Yes.

xx CROSS EXAMINATION

BY MR. VELIE:

Q Mr. Otkiss, I believe you have already told us you are Mr. Natelli's partner, is that correct?

A That's correct.

Q Is it also fair to say you consider yourself his friend?

A Yes.

Q Mr. Otkiss, as an SEC review partner you were aware.

weren't you, of what the lawyers sometimes call the case of Fischer vs. Kletz? Judge Tyler decided that case, but you might know it as the Yale Express case.

A Well, I have some recollection of it but I don't have any detailed knowledge of it.

Q You were aware, were you not, that in the Yale Express case Peat, Marwick and Mitchell had to pay damages to various people who sued them because --

MR. STILLMAN: Your Honor, that is not the way it happened.

THE COURT: I quite agree.

MR. VELIE: I will restate the question.

THE COURT: I will ask the jury to disregard that. I don't really see, in any event, what that case has to do with our case.

Q Let me put it to you this way:

That case had in it, didn't it, a little lesson with respect to what to do if you discover that previously issued reports are no longer reliable? Isn't that fair to say?

A I can't even answer that. I assume so, but I can't answer it directly.

Q Let's go on to things that you talked about in your direct examination.

Letme set a little background. Your firm is now a party in civil litigation surrounding the matters surrounding this case, isthat correct?

A I believe so, yes.

Q It is being sued by various people, is that correct?

A Just what I have heard and have been told. I have no direct knowledge.

Q The suits, if successfuly, might mean that the company would have to pay out damages, is that correct?

A I would assume so.

Q Peat, Marwick, Mitchell and Company?

A I would assume so.

Q It might also mean suspension by the SEC for some period of time?

A Well, I would have to leave that to be answered by the SEC.

Q Mr. Otkiss, you testified on your direct and you looked at Government's Exhibit 17 in evidence. The first thing you said was you weren't sure you had seen that particular draft, you had seen a draft. Do you recall that testimony?

A Yes.

Q That is so, isn't it?

A That's correct. I was referring to this specific document.

Q Right.

In fact, you didn't see any draft at all, did you, when you talked to Mr. Natelli, until after the nine-months figures were inserted in the proxy, is that correct?

A I don't recollect that, no. I am sorry.

Q Let me read to you something from your grand jury appearance on November 14, 1973.

"Q Can you tell us approximately when you had these conversations with Mr. Natelli?

"A Again, I would guess basically, but it would have been in mid-August or something of that nature, it would have been after the nine-month figures had been included in the proxy statement."

Do you recall giving that answer to the grand jury?

A If it is there I did, but I don't recall it in that specific.

Q Is that the truth of the matter, that you saw it after the nine-month figures went in?

A No, I cannot say that, I cannot make that statement.

Q Mr. Martin showed you Government's Exhibit 17B.

So that the jury knows what it is we are doing, it is again Chart No. 10.

Mr. Otkiss --

MR. MARTIN: Your Honor, sorry to interrupt, but at this point, given the fact that Mr. Otkiss is being confronted with his grand jury testimony, a document I have not seen, I would like an opportunity -- I think Mr. Velie agreed -- to see it so I can see how compl~~e~~ete it is.

THE COURT: All right.

Again, I just want to make sure of something else here. Does Mr. Otkiss have 17B, because he can't possibly see this chart.

MR. VELIE: Yes, he does, your Honor. It is right before him.

THE COURT: You have it.

THE WITNESS: Yes.

MR. VELIE: Thank you, your Honor.

Q You testified on your direct examination that you discussed that very footnote there with Mr. Natelli, is that correct?

A That's correct.

Q That is your best recollection?

A That is my best recollection, yes.

Q Do you recall being in the grand jury on that same day, November 14, 1973?

A Yes.

Q Being asked now, "Specifically, do you recall having had any discussion with Mr. Natelli on the subject of the footnote that is crossed out and the figure for the retroactive adjustment which is also crossed out on this proof page?

"Answer. No. Not specifically."

That is so, isn't it?

A Yes, but what I said earlier is correct, we discussed the substance of that footnote and the adjustment.

Q But you don't recall actually seeing what had been crossed out in --

A No, the cross out I may not have seen. That may not have been on my copy. But the substance of the footnote and the substance of the adjustments we discussed.

Q And I believeyou have told us that what Mr. Natelli

told you about the substance of those adjustments was, there was one specific situation involving one salesman's problem, is that about it?

A That and the deferred taxes.

Q And the deferred taxes?

A That's correct.

Q As you told us, your recollection is he told you five, six, $700,000.

A Something of that magnitude.

Q Did Mr. Natelli point out to you that in the 1968 report after tax earnings of $388,000 were achieved with these unbilled accounts receivable, but that without them there would have been a loss? Did he point that out to you?

A No, we did not discuss that. We had already agreed that the accounting was appropriate.

Q You had?

A Yes.

Q Well, did he tell you then that in the intervening 18 months the $1.7 million of unbilled accounts receivables he booked and an additional 1.8 million, totaling $3.3 million of unbilled accounts receivable, had been booked? Did he point that out to you?

A Why would he for 18 months? I don't understand the 18 month period.

Q Did he tell you, sir, that of that $3.3 million over $2 million had been written off as no good and uncollectible?

A At the time we reviewed this, I don't even know if he was aware of it. You speak of a period of 18 months. I'm talking about August of 1969.

Q There is evidence before this jury, Mr. Otkiss, that Mr. Natelli knew that in June.

MR. MARTIN: Objection, your Honor.

THE COURT: I would agree that that certainly is objectionable as to form.

MR. VELIE: Very well. The jury will recall what the evidence is.

I withdraw my statement.

MR. MARTIN: I object, your Honor, to Mr. Velie telling the jury what they are to do.

THE COURT: In any event, he's going to rephrase the question, we hope.

Q Did Mr. Natelli tell you that he considered the entire balance of $3.3 million to be uninforceable contracts?

A No.

Q With respect to this being one salesman's problem, did Mr. Natelli point out for your edification that that one salesman had a problem in the tune of $670,000 worth of the

contracts but that another salesman had booked a contract for a million dollars which had been written off?

A I have no recollection.

Q That --

A Excuse me.

Q Go ahead.

A Are you referring to a specific contract?

Q Yes, a contract for the Pontiac Division of General Motors.

A We had a discussion of the Pontiac contract. As I understand it, at the time it was not a matter of something that was written off, it was a matter of something that was not a written commitment at the time.

Mr. Natelli informed me that he would not permit them to book that type of contract.

Q Is that whathe told you?

A That's correct.

Q Thank you, sir.

Did he tell you that as that particular contract was disallowed, the same salesman came up with a new one in a tremendous amount never previously mentioned, that all of this took place at 3 a.m. in the morning at the printer's plant while it was time to print the proxy numbers?

MR. MARTIN: I object to the form of the question,

your Honor.

THE COURT: Yes, I think I would ask you to rephrase that and condense it a bit.

MR. VELIE: Yes, sir.

Q Did Mr. Natelli tell you that the same account executive attempted to rephrase the Pontiac commitment with another one?

A I haveno recollection of that.

MR. MARTIN: Objection.

THE COURT: I will allow that.

You say you had no recollection of that?

A That's right.

Q He didn't tell you then anything about an early morning session at the Pandick Press in which that happened?

A I have no recollection of it.

Q Were you aware, sir, that the tax credit Mr. Natelli was talking about appeared exactly in time and exactly to the penny in the amount to absorb the profit write off of the three contracts he was talking about with respect to the one person he told you about?

MR. MARTIN: Objection to form. It is an inaccurate statement.

THE COURT: Without trying to suggest to the jury whether it is accurate or inaccurate, I will let that stand.

A Will you repeat it, please.

THE COURT: Let me correct myself. I think in fairness to Mr. Otkiss, the question ought to be rephrased from another point of view. See what I mean?

MR. VELIE: Yes, your Honor.

Q Were you aware, sir, that contracts which Mr. Natelli did tell you about, three of them, amounted to $678,562 of revenues exactly?

A I can't say that, no. I don't think I knew the precise number.

Q And related costs in a precise number of 489,812?

A I can't speak to the precise number. I knew there were offseting costs, but I don't know what the precise number was.

Q Did he tell you the circumstances under which the tax credit amounted to exactly the amount of profit being written off to the penny?

MR. MARTIN: Objection.

THE COURT: I think this is a fair question. In other words, he's asking you to assume, Mr. Otkiss, that these are the exact figures. Obviously, as you say, you can't recall. Assuming that they were as he states them, do you recall any deferred tax figure as being somewhere in the neighborhood of this amount written over on the blackboard

$188,750?

A Yes, I do.

Q Did he tell you the circumstances and explain to you how it came to be that they turned out to be the exact amount?

A We had no discussion of that.

xx REDIRECT EXAMINATION

BY MR. MARTIN:

Q Mr. Velie asked you some questions, Mr. Otkiss, about the proof that you reviewed.

Have you had occasion over the last few days to review your diary to determine approximately when it was that you spent time working on these proofs?

A I can give you -- I have my diary with me. I can give you the dates.

Q May we have it, please?

MR. MARTIN: Can we have this marked.

(Defendant Natelli Exhibit Q marked for identification.)

Q Would you look at your diary, sir, and see if that refreshes your recollection as to --

A According to my diary, the first time I had a charge to National Student Marketing was on August the 12th. I had an hours timethen. On the next day I spent the whole

day, and I can only assume that was reviewing the proxy that was available at that point in time.

Q So you were reviewing a proxy prior to August 14, is that correct?

A That's correct.

Q Mr. Velie asked you whether you recalled that Mr. Natelli toldyou certain facts.

Did you, Mr. Otkiss, ask Mr. Natelli all of the questions that you felt you wanted to ask about the item he was raising with you?

A Yes, I did.

Q Did he in any way give you evasive answers about anything?

A None that I can recall.

Q Did he answer as best you can recall, directly any questions you asked him?

A Yes.

Q Did he ever ask you to cover up a thing?

A No, he did not.

MR. MARTIN: Thank you.

THE COURT: Mr. Otkiss, before you leave could I ask:

Doyou recall anyone bringing to your attention, let's say on August 13, 12 or 13 or sometime in early

August, the method of accounting which this company was then on?

THE WITNESS: No, I -- my memory, sir, I raised the question when I read the footnotes.

THE COURT: What were you told?

A I was told that this was an attempt to match -- this was the earning process that they earned most of their revenue during the billing of the period. I don't recall the specifics of it, your Honor.

THE COURT: What I'm trying to get at was whether or not you had any understanding that this was a form of percentage of completion --

A Yes, sir.

THE COURT:--Accounting.

THE WITNESS: Yes, sir. I was aware of that.

THE COURT: Could you tell the Court and jury your working definition of that method of accounting?

THE WITNESS: Percentage of completion method is basically a method of recognizing revenue and income as work is performed and a contract. It is naturally applied to long term contracts, but I wouldn't say that it must in all cases.

THE COURT: Would you agree, sir, that in order for this method of accounting to be workable and appropriate, it presupposes adequate records of expenses and as precise

estimates of completion with back up records behind those estimates as can be achieved?

A I would only take one exception to that, your Honor.

THE COURT: What's that?

THE WITNESS: That's the precise measurement that you referred to.

THE COURT: All right.

THE WITNESS: Because in all contracts, long term contracts, obviously you can't measure the stages of completion that precisely. Naturally as you get a better grip on the stages of completion, you adjust that on an on-going basis.

THE COURT: All right. I understand.

THE WITNESS: Other than that, generally, yes, you would have to have good records to support the costs incurred and the estimated costs.

THE COURT: Of course I accept your correction about precision. Nevertheless, from time to time as work goes forward, I would assume from a proper accounting point of view that you would want to see as intelligent and as careful estimates as possible about completion, even though we have to recognize that obviously, as you point out, they can't be precise.

A That's correct, sir.

THE COURT: Very good.

Thank you, sir.

Gentlemen, forgive me. If my questions have triggered any more from you, please say so.

MR. MARTIN: None from me, your Honor.

MR. STILLMAN: Not me.

MR. VELIE: No, your Honor.

THE COURT: Thank you, Mr. Otkiss. You may be excused.

(Witness excused.)

MR. MARTIN: William Colona.

W I L L I A M C. C O L O N A, JR., called as a witness by the defense, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. MARTIN:

Q Mr. Colona, by whom are you employed, sir?

A I am employed by Peat, Marwick, Mitchell & Company in Washington, D.C.

Q In what capacity are you presently employed by Peat, Marwick, Mitchell & Company?

A I am an audit manager.

MR. MARTIN: Your Honor, for the record, I make the same application that I made with regard to Mr. Otkiss.

THE COURT: I now understand you and I make the same ruling.

MR. MARTIN: One trip to the side bar is saved anyhow.

Q Directing your attention to the period the fall of 1969, what was your employment at Peat, Marwick & Mitchell, sir?

A I was an audit supervisor at that time.

Q Did you have occasion during that time to be assigned to the audit for the period ending August 31, 1969

of National Student Marketing Corporation?

A Yes, I did.

Q What was your responsibility with regard to that audit, sir?

A My responsibility basically was to supervise the conduct of the audit engagement and instruct the senior in charge of the engagement and the staff in the field.

Q Who was the senior in charge of the engagement?

A Mr. John Johnston.

Q Did you replace someone on that engagement?

A Yes, I did.

Q Who was that?

A Mr. Joseph Scansaroli.

Q Who did you work under?

A Mr. Natelli.

Q Do you see Tony Natelli and Joe Scanscaroli here in the courtroom?

A Yes, I do.

Q I show you defendant Natelli Exhibit N, which for the record is all in evidence with the exception of the first page, and ask you to look at the first page and tell us, sir, if you can identify that.

A The first page is a memorandum to me from Mr. Natelli.

Q At the time you received that was the rest of the document that is attached to that attached to the memorandum?

A Yes.

Q When approximately was this received by you?

A I would say it would be around the 6th of October 1969.

MR. MARTIN: Your Honor, at this time I would offer the rest of Natelli Exhibit N.

THE COURT: I think you may have already said this, Mr. Colona. You are identifying this as a note in Mr. Natelli's hand?

THE WITNESS: Yes.

THE COURT: All right. Any objection to receiving the first page, Mr.Stillman or Mr.Velie?

MR. VELIE: Your Honor, I don't remember the document. I better look at it.

Oh, no, I have no objectionto this. I believe this first page was already in.

MR. MARTIN: No.

THE COURT: That's right.

MR. MARTIN: We redacted the first page although

I did not physically redact.

THE COURT: Correct.

MR. VELIE: Now we know what it is and there is no objection.

MR. MARTIN: It doesn't have to be marked because it was marked.

Now I can show the ladies and gentlemen of the jury the first page of Natelli Exhibit N. You may recall the rest of the document was a document identified during the testimony of Mr. Johnston. The first page is a note.

(Mr. Martin read from Defendant Natelli Exhibit N in evidence to the jury.)

Q Have you seen that swirl before?

A Yes, I have.

Q That is Mr. Natelli's initials?

A Yes, they are.

Q Did you have any conversation about Natelli Exhibit N with Mr. Natelli at that time?

A Yes, I did, or shortly thereafter.

Q Would youtell us, tell the ladies and gentlemen of the jury,that is, what that conversation was as best you can recall. First, where did it take place?

A It took place in our offices in Washington, D.C.

Q Who else was present?

A I believe it was just Mr. Natelli and myself.

Q Would you tell us now what Mr. Natelli said to you and what you said to him as best you can recall.

A Mr. Natelli was concerned over the contracts which gave rise to this tailored audit program to be utilized in conjunction with the August 31, 1969 audit of the contracts.

He said that we had experienced problems with these type of contracts in the past and that all the contracts should be in writing and that we were going to confirm 100 per cent of those contracts.

Q Mr. Colona, did there come a time when you became aware that Peat, Marwick, Mitchell was to furnish a comfort letter in connection with a merger between National Student Marketing and the Interstate National Insurance Company?

A Yes, I did.

Q Do you recall when it was that you -- let me see if I can give you some help.

MR. MARTIN: Can I have this marked as the next exhibit for identification.

xxx (Defendant Natelli Exhibit R was marked for identification.)

Q I place before you Natelli Exhibit R for identification. Can you tell the ladies and gentlemen of the jury what that is, please?

A This booklet is a summary calendar in which I record my time. It is basically a time diary.

Q A time diary?

A Yes.

Q Can you use that to refresh your recollection, sir, as to when you began working on this comfort letter?

A I began working on this comfort letter on October 17, 1968.

Q As far as the responsibility for preparing that comfort letter, what was the so-called chain of command within Peat, Marwick, Mitchell?

A I would normally draft the comfort letter and have it subject to Mr. Natelli's review and he would eventually have to sign it as a partner in the firm.

Q With regard to any figures that might go into the comfort letter, who would you consult about that?

A Mr. Johnston, the audit senior.

Q Did you have any conversation with Mr. Natelli that you can recall prior to the time the comfort letter was issued?

A Yes. About the following week after this

October 17th date Mr. Natelli had reminded me that we should be cognizant of any audit adjustments which we may have been aware of at that point in time during our August 31, 1969 audit which would have effect on the unaudited May 31, 1969 numbers which were reported in the proxy statement.

Q What did you sayto him, if anything, that you can recall?

A As I recall, I indicated to him that I would speak to John Johnston about this and that we would attempt to summarize our work to date in order to see if there was any impact on the May 31 numbers.

MR. MARTIN: Could I have Government Exhibit 26, please, and 34.

Q I am going to show you what has been received in evidence as Government Exhibit 26, Mr. Colona, and ask you, sir, are you familiar with that document?

A Yes, I am.

Q What is that document, sir?

A This document is I believe one of the initial drafts of the items to which we felt at that time should be reflected retroactively to May 31, 1969, to be included in the comfort letter.

Q Who drafted that document, sir?

A I did.

Q You will note in that document Item 2 refers to the adjustment of receivables. Who chose that language to describe that situation?

A That was my language.

Q Did Mr. Natelli ever suggest to you that you should use the term "receivables" and not "unbilled receivables"?

A No, he did not.

Q I show you Government Exhibit 34, Page 3276 and ask you, sir, to look at that schedule and tell us what that is.

A This is a schedule of adjustments to prior years commitments. From this work paper we derived the figures which eventually went into the comfort letter.

Q The draft that is Government Exhibit 26 refers to adjustments to receivables in the amount of $300,000, sir. Was that the correct amount, sir?

A No, it was not.

Q What should the correct amount be?

A The correct amount should be approximately $200,000.

Q Can you tell the ladies and gentlemen of the jury how that amount is derived from the document in front of you, Government Exhibit 34, Page 3276?

A That figure is derived by taking the receivables which were recorded or written off -- excuse me -- subsequent to May 31, 1969, which aggregated approximately $372,000, and the related accrued costs of approximately $166,000, which netted down to the approximately $200,000 adjustment which was included in the comfort letter.

Q That was the amount, $200,000, that appeared in the final comfort letter, which is now Natelli Exhibit K, is that correct?

A That is correct.

Q The contracts that were written off making up that $200,000 receivable item, did that $200,000 item include profits on a contract or three contracts with Syntex?

A Yes,it did.

Q Have you since learned whether or not the Syntex contracts had in fact already been written off in the proxy statement for May 31, 1969?

A That is my understanding.

Q So that your comfort letter was in error, is that correct?

A That's correct.

Q What was the amount that should have been shown in the final comfort letter for the writeoff of receivables?

A Approximately 149,000.

Q Directing your attention to Wednesday, October 29 and Thursday, October 30, do you recall where Mr. Natelli was on those days?

A On October 30, Mr. Natelli was at home sick.

Q Did you have occasion to speak with him at his home that day?

A Yes, I did.

Q At what time did this conversation take place as best you can recall?

A I talked with Mr. Natelli in the evening of that day.

Q Would you try and tell us now -- this was a telephone conversation, is that correct?

A Yes, it was.

Q Just you and Mr. Natelli on the phone?

A That's correct.

Q Would you tell the ladies and gentemen of the jury what you said to Mr. Natelli and what he said to you as best you can now recall it, sir.

A I informed Mr. Natelli that we had come up with substantial adjustments which would affect the unaudited May 31, 1969 figures which were included in the proxy statement and that these adjustments approximately made $800,000.

Mr. Natelli then asked me to call Mr. Otkiss, who at that time was an SEC reviewing partner in our Philadelphia office, first thing in the morning and inform him of the situation and that he would be in some time in the morning, the following morning.

Q Did you call Mr. Otkiss the following morning?

A Yes, I did.

Q At any time you discussed these matters relating to this comfort letter with Mr. Natelli did he tell you that he wanted you to cover up any adjustments because he might have some personal problems if any of this came to light?

A No, he did not.

Q Did he ever ask you to do anything but a fair and honest job in the work you were doing?

A No, he did not.

Q Did he ever ask you to do anything improper?

A No, he did not.

THE COURT: Mr.Stillman?

MR. STILLMAN: I have none, your Honor.

CROSS-EXAMINATION

BY MR. VELIE:

Q Mr. Colona, you did your best to put all of the adjustments of which you were aware into this letter, is that correct, Government Exhibit 26?

A That is correct.

Q Did Mr. Natelli suggest additional adjustments to you of any kind?

A Not to my knowledge.

MR.VELIE: Thank you.

THE COURT: Is that it?

Thank you, Mr. Colona.

You may be excused.

(Witness excused.)

6 PM

MR.MARTIN: Thomas Holton.

T H O M A S L. H O L T O N, called as a witness by the defense, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. MARTIN:

MR. VELIE: I have asked Mr. Martin to bear with me for just a moment while I locate a paper which would be of assistance to me in this witness' examination.

(Pause.)

Q Mr. Holton, what is your occupation, sir?

A I am a certified public accountant.

Q What firm are you associated with?

A Peat, Marwick, Mitchell & Company.

Q In what capacity, sir?

A I am a partner in the executive office, the Department of Professional Practice, accounting and auditing and I am chairman of the firm's SEC reviewing partners.

Q Did you hold that position in 1969?

A Yes, sir, I did.

Q Is Tony Natelli your partner?

A Yes.

Q Was then?

A Yes, he was then.

Q Your friend?

A Yes.

Q Mr. Holton, did there come a time when you had some association with the work that Mr.Natelli was doing with the National Student Marketing Corporation?

A Yes, sir.

Q When for the first time did you become associated with the National Student Marketing engagement as best you can recall?

A It was either late 1968 or early 1969, I believe.

Q Do you recall the circumstances that first brought National Student Marketing Corporation to your attention?

A It was a telephone conversation, I believe it was by telephone, with Tony Natelli about a problem, I guess you would say a disagreement he had with a client about the accounting on a new acquisition that National Student Marketing had had.

Q Do you remember the name of the client?

A The company was New England Travel or New England Travel Service, something like that.

Q Do you remember what Mr. Natelli told you about this particular problem?

A The problem was that the client wanted to recog-

nize income on some tours, I believe they were, educational tours, something like that, that would take place the following summer,and they wanted to recognize the income in the fall when the deposit was made, to sign up for the tour to take place the next summer.

Q Did Mr. Natelli tell you what position he had taken with the company?

A Yes. He did not think it was appropriate to recognize the income at that time.

Q Did he tell you why he was calling you?

A Well, he had had apparently considerable discussion with the client and the client wanted to -- not necessarily me, I suppose, but to have a chance to talk to somebody in the Department of Professional Practice about the method of accounting.

Q Is it fair to say the client was trying to go over Mr. Natelli's head?

A Well, the client didn't go directly. As I recall it, it was probably asking him and he agreed to get someone to take a look.

Q Did you have occasion to meet with the client?

A Yes.

Q What was the result of those discussions?

A We had one discussion at night in their

offices in Washington, and we heard the story about how all this takes place. I suppose we -- well, we must have agreed at that time to meet again with him in our office in New York at 70 Pine Street, because we did have another meeting on it and discussed it again for most of the day, including some discussion of the position some other firm might take, and we concluded in the final analysis that we could not recognize income, as Tony thought, in the first place.

Q The conclusion was the same that Mr. Natelli had reached originally, is that correct?

A I don't recall any variation, the essential conclusion.

Q You said there was some reference to some opinion from another firm.

Was that opinion the same as the one that you and Mr. Natelli came to?

A Well, during the discussion we were told that Haskins & Sells would agree to take up the income in the early stages and we did talk to someone, but not a partner, during the day, but it didn't really make any difference to us what that person thought. We don't ignore completely what someone else thinks, but in that case of course we did conclude that it didn't make any difference.

Q You did conclude they could not record any such income, is that correct?

A Right.

Q Directing your attention to October of 1969, did you have occasion to become involved with a comfort letter that Peat, Marwick, Mitchell was to issue in connection with a merger between National Student Marketing Corporation and the Interstate National Corporation?

A Yes, I did.

Q When did you first become involved with this comfort letter situation?

A About noon on October 31, 1969.

Q Can you recall the events of that day for us, sir?

A Well, I got a conference call from Tony Natelli and Lee Otkiss at about twelve o'clock that day outlining to me that the merger was to take place, there was to be a closing that afternoon in New York at the offices of White & Case, that the company had been advised that our comfort letter that had to be delivered for purposes of closing was going to say that the --

Q Let me interrupt you.

The comfort letter was to deal with what period, sir?

A The comfort letter was to deal with the --

primarily with the unaudited financial statements for the nine months ended May 31, 1969.

Q Would you continue. What were you advised at the time?

A I was told that the client had been told that the comfort letter would say that the unaudited nine months financial statement should be adjusted and that our people had been told or Natelli had been told that they were going to goahead and have the closing anyway in spite of the comfort letter, pointing out the need for these adjustments to the financial statements.

I was also told that there was some problem getting the comfort letter down from Washington for some reason or other.

That is basically what happened on that telephone conversation.

Q What did you do? Did you give any instructions or discuss with Mr. Natelli what he should do or what you would do with regard to this matter?

A Well, the comfort letter draft was to be sent to New York by some means. It turned out it was sent through a stenographer, secretary at White & Case, and then brought down to me.

We also agreed that we should talk to counsel

about what we should do about these circumstances.

Q Did you consult with counsel?

A Yes. It was after lunch before I could reach our counsel, because he was not there that day. He was at home taking a day's vacation. Neither was his secretary. I didn't find out where he was until after lunch.

Q What is his name, sir?

A Victor Earle.

Q Did you talk to Mr.Earle on that day?

A Several times on the telephone during the afternoon.

Q Do you recall what your next conversation with Mr.Earle was?

A Well, I can't recall precisely the sequence, but early in the discussions I had outlined to them that I understood that the lawyers involved for National Student Marketing and Interstate thought there were no legal problems in going forward with the merger and in spite of the fact that the comfort letter said the financial statements for May 31 should be adjusted. He suggested that we get that opinion in writing because he was concerned about going forward with the merger in spite of the comfort letter saying this.

I had -- that was the early discussion with

Mr. Earle.

Q What did you do after talking to Mr. Earle?

A I talked to J. Epley at White & Case and the general counsel for National Student Marketing.

Q Does the name Davies refresh your recolldction?

A John Davies,and possibly counsel from Chicago who was on the line, but I am not sure about that.

In the discussions -- I talked to him before that, but after I had asked for a written opihion he told me that neither theChicago firm nor the New York firm would give such a written opinion, although they could understand why they would go ahead and close the deal anyway.

Well, I don't know how many conversations we had during the afternoon between me and Victor Earle, between me and Tony Natelli in Washington and between me and the lawyers, also some conversations from Tony to the lawyers.

Q I show you Natelli K in evidence, which has been identified as the final comfort letter and some covering letters that you sent out,sir (handing).

Were any of the paragraphs in the comfort letter added as the result of the discussions that you had with Mr. Natelli and Mr. Earle on this day? And would you tell us how those additions were communicated to the parties at the closing?

MR. VELIE: Wait a minute. I object to the form of that question simply because, Mr. Martin, I believe it suggests that Natelli Exhibit K was somehow delivered at the closing. If you will solve that for me, I have no objection.

Q Was Natelli Exhibit K delivered at the closing, sir?

A At the time the transaction was closed?

Q Right, was that delivered at that time?

A A draft of the letter had been in their hands since twelve, one o'clock.

Q But the final comfort letter was not, is that correct?

A The final comfort letter was not.

MR. VELIE: Thank you.

Q The final comfort letter was sent by you on November 3, is that correct?

A No, the final comfort letter was sent by me by messenger late in the day of October 31.

Q The covering letter of November 3 is a letter you sent to whom and when?

A The covering letter on November 3 is to each member of the board of directors of National Student Marketing Corporation and Interstate National Corporation. That was

Monday following Friday.

Q You said there was a draft that had been sent down to White & Case. Did you have any discussions with people at White & Case about additional paragraphs to be added to that draft?

A Yes.

Q What were those discussions as best you can recall?

A There may have been a slight change in the numbers, but I don't think so during that afternoon. But the essential changes that were made were to add two paragraphs to the letter.

Q Were they both added at the same time or at different times?

A No, they were not added at the same time. The first one was added mid-afternoon or earlier, I suppose.

Q What was the paragraph that was added first in the mid-afternoon?

A It was the fourth from last paragraph in the comfort letter.

Q Would you read that to the ladies and gentlemen of the jury so they know what we are talking about.

A The fourth from the last paragraph says:

"Your attention is called, however, to the

fact that if the aforementioned adjustments had been made at May 31, 1969, the unaudited consolidated statement of earnings of National Student Marketing Corporation would have shown a net loss of approximately $80,000. It is presently estimated that the consolidated operations of the company as it existed at May 31, 1969, will be approximately a breakeven as to net earnings for the year ended August 31, 1969."

Q After that paragraph was added did you have occasion to talk to anyone at White & Case or at the closing about an additional paragraph to be added?

A Yes,we had some discussion about that paragraph, too, and --

Q What was the discussion about that paragraph first?

A Well, the discussion essentially was that the lawyers thought it was unnecessary that you could take what we had already drafted and subtract the numbers and get the same answer. I told them we had concluded for emphasis -- we wanted to be sure no one misunderstood it -- we were going to put it in anyway.

Q Then did you have occasion to again discuss an additional paragraph with the people who were to be at the closing?

A Well, after these numerous conversations during the afternoon in Washington to me and with Victor Earle and so forth, we finally concluded after we could see that they apparently were going to close the deal anyway, we decided to add another paragraph.

Q What was that, sir?

A That was the third from last paragraph that said, "In view of the above-mentioned facts, we believe the company should consider submitting corrected interim unaudited financial information to the shareholders prior to proceeding with the closing."

Q As the head of the SEC Reviewing Committee of Peat, Marwick, Mitchell, do you know whether the company could submit new unaudited financial statements to its shareholders without notifying the SEC?

A Well, I am not a lawyer but I believe that would require a new proxy statement and so forth.

Q What happened when you delivered the message about that additional paragraph to the people at White and Case?

A When I told them we had decided to put in this additional paragraph and finalize our letter -- this was about 4:30 -- I was told by Jay Epley that the merger had been closed and the people in Chicago had already left his office.

Q Did you have any discussion with any of the people at Peat, Marwick after that about what other steps Peat, Marwick Mitchell might take?

A Yes, I did. We were quite astonished that this would happen, and in my experience it never had happened, and so was our counsel concerned about it, so I discussed it with him, I believe I talked to Tony Natelli about it. So it was 4:30 when I talked to Jay Epley.

I got the letter finalized, sent it by messenger -- I think I sent it by messenger -- anyway, I sent it, with a

letter of transmittal, which is also here, saying that we would consult further with counsel and would advise them Monday morning if we were going to do anything else.

Q Did you have additional discussions with counsel?

A Yes, that day, sometime after 5 o'clock, we talked about it.

Q What were those discussions? What did Mr. Early say, what did you say? Was anybody else --

A Well, we talked about the possibility of our having an obligation to go to the SEC to report this, we talked about our requirements under our Code of Professional Ethics, the confidentiality, some state laws on confidentiality, not revealing confidential information.

Well, it was too late to call the SEC when we were talking about that anyway and we decided to wait until Monday morning and let counsel think about what we should do and for us to talk about it some more, which we did over the weekend, and Monday morning we did decide to send copies of it to all directors of both companies.

Q Was a decision made not to bring this matter to the attention of the SEC?

A Counsel decided that we shouldn't, yes.

Q That is, Mr. Earle?

A Yes.

Q Did he tell you his reasons for not doing that?

MR. VELIE: I am going to object at this point. We have who did it and I believe that is sufficient.

THE COURT: I would agree. We have heard from Mr. Earle.

MR. MARTIN: I have no problem, your Honor. I just want to get both sides of the story. It is perfectly all right with me to withdraw it.

Q Did you prior to sending that letter to all the directors of both corporations, as you did on you toldus, I believe, the following Monday, did you have occasion to speak with Mr. Natelli?

A Yes, I did.

Q Did you tell him what you planned to do at that time, sir?

A Yes, I -- well, I probably talked to him before the final decision, but I am not sure.

Anyway, he was spoken to.

Q In any of the conversations you had with Mr. Natelli about this comfort letter, the various possibilities for action, what Peat, Marwick Mitchell planned to do, did Mr. Natelli ever suggest to you or hint to you that perhaps Peat, Marwick should do something less than it thought

appropriate because he might have a problem if any of this stuff came to light?

A None whatsoever.

Q Did he ever ask you to cover up a thing, sir?

A Beg your pardon.

Q Did he ever ask you to cover up a thing?

A No.

MR. MARTIN: No further questions, your Honor.

MR. VELIE: I see the hour, your Honor, but perhaps we cansave Mr. Holton a trip if I ask my two or three questions briefly.

THE COURT: Fine. I was just going to ask if we couldn't do that. I unfortunately have to go to a meeting at 4:30. Can you finish quickly?

MR. VELIE: Yes, your Honor, I can.

MR. MARTIN: I know Mr. Holton has to be in Louisiana tomorrow, so he would appreciate it.

THE COURT: All right.

xx CROSS EXAMINATION

BY MR. VELIE:

Q Good afternoon, Mr. Holton. Just to place this in context, the fourthfrom the bottom paragraph, is that how we have been caling this thing in the comfort letter which you read aloud to the jury, the one which says in effect

there would be a break even for the year and so on?

Do I have that right?

A Yes, sir.

Q You had told Mr. Natelli that that had to be in the comfort letter, is that correct?

It was your idea communicated to Mr. Natelli? Do I have that right?

A I had so many telephone conversations that afternoon that I can't say for sure that -- well, I wouldn't say for sure I said absolutely it had to be done. We discussed the thing.

Q I am just trying to see if we can straighten out whether it was your idea or his idea. It was your idea, wasn't it?

A I can't say for sure. It could very well have been.

MR. VELIE: Government's Exhibit 67 please, for identification.

xx (Government's Exhibit 67 marked for identification.)

Q Mr. Holton, this is your memorandum of November 5, 1969, isn't it?

A Yes, that looks like it.

Q You prepared that very shortly after the events

which you have been telling us about, right?

A Right.

Q While memory was fresh?

A Well, yes.

Q Do you recall writing down in your memorandum "previously I had told Tony Natelli to advise the client that the fourth from last paragraph must go in the comfort letter"?

A Well, that sounds like what happened then.

Q Thank you.

The other paragraph which didn't get in on time, the one you told us about where they should resolicit it, the shareholders, again, that idea came from your end, isn't that right, rather than from Mr. Natelli?

A I am rather confident that Vic Earle suggested that.

Q Vic Earle suggested that?

A Because it never happened in a comfort letter in my experience.

Q Do you recall - and you can look through this if you would like to help yourself -- do you recall that Mr. Natelli suggested adding anything to that comfort letter?

A As I said earlier, I don't recall whether there were some other changes in the other parts during the day.

If there were they must have come from him because I couldnt' have made them.

Q I believe we don't have any evidence before us that there were, but why don't you just take a look in there and see if you made any record of Mr. Natelli suggesting that anything additional go into the comfort letter.

A Well, I haven't read the memo in detail, but I don't recall anything like that.

MR. VELIE: Thank you, your Honor.

xx REDIRECT EXAMINATION

BY MR. MARTIN:

Q Did Mr. Natelli ever object to any of the suggestions that you made for changes in the comfort letter?

A No.

Q Did he express his agreement with what you were doing?

A Yes.

THE COURT: Thank you, Mr. Holton.

MR. STILLMAN: Just one, your Honor.

xx RECROSS EXAMINATION

BY MR. STILLMAN:

Q How many years have you been at this, sir, as a CPA?

A 25 years, 24 years.

Q This is the first time you had a kind of negative comfort letter, that is, a comfort letter that wouldn't give comfort, is that what you said?

A Well, the first time that paragraphs like those two had been put in.

Q And the whole thrust of this comfort letter came from Mr. Natelli down in the Washington office, is that right?

MR. VELIE: Now wait a minute.

THE COURT: Sustained as to form.

Q The whole idea to all the information insofar as the adjustments were concerned, the negative adjustments, came out of the Washington office, is that right?

A Absolutely.

MR. STILLMAN: Thank you.

MR. VELIE: Your Honor, I object to the leading, and we just heard Mr. Colona say who did it.

THE COURT: It is sufficient unto the day.

Thank you, Mr. Holton. You may be excused, sir.

(Witness excused.)

THE COURT: Ladies and gentlemen, we will suspend now, as you know, until tomorrow. 10 o'clock. You know we will quit before luncheon tomorrow.

(Adjourned to 10 a.m., November 5, 1974.)

United States of America

vs.

74 Cr. 43

Anthony M. Natelli and
Joseph Scansaroli

New York, New York
November 7, 1974 - 10:00 A.M.

(Trial resumed.)

(In open court; jury present.)

THE COURT: Good morning, ladies and gentlemen.

Mr. Martin.

MR. MARTIN: Call Anthony Natelli.

A N T H O N Y N A T E L L I, called as a witness by the defense, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. MARTIN:

Q Mr. Natelli, what is your present occupation, sir?

A I am a CPA, a partner in the firm of Peat, Marwick, Mitchell, in theWashington office.

Q The normal rules, Mr. Natelli. Try and keep your voice up so that everybody can hear you.

A Right.

Q Talk to everybody in the back of the room. Perhaps that will help.

Would you tell the ladies and gentlemen of the jury something about your background, Mr.Natelli.

A I was born across the river in Jersey City in 1936, attended public schools thrcugh the grammar and high school level, after which I attended St. Peter's College, graduated in 1957 with a B.S. degree with a major in accounting.

Married, Trudy and I have been married for 18 years. We have five children, three boys, two girls. The oldest is a girl, Nancy, 17. The youngest is a boy, who will be ten next week.

Q Upon graduating from college what did you do?

A Immediately upon graduation from St. Peter's I joined the certified public accounting firm of Peat, Marwick, Mitchell in their Newark office.

Q Would you tell the ladies and gentlemen about your career with Peat,Marwick.

A I started with the firm in our Newark office as an assistant accountant and was there for approximately six years. During that period I was promoted from time to time, to the point that I was a supervisor in 1963, when

the firm asked me to transfer to our Washington office. I was in Washington for two years,where I was promoted during that time to a manager. The firm then asked me if I would transfer for a short period of time, several years, to Europe, where I was asked to take charge and I did transfer and take charge of our Milan and Rome offices in Italy as the partner in charge of our Italian firm.

I then returned to Washington at the request of the firm in July of 1968 to become the managing partner of that office.

I have been there in Washington since that time.

Q What were your responsibilities upon your return, sir, as the head of the Washington office of Peat, Marwick, Mitchell?

A Well, the office at that time had essentially an audit and tax practice. It was mostly an audit practice. We had somewhere between 40 and 50 personnel, as I recall. There were two partners besides myself when I returned, the partner who had been in charge of the office and was beginning a period of what we would call phasing out toward retirement -- I was actually his successor -- and we had a partner in our tax department, George Terry.

My responsibilities were the entire matters of administration and management of the office from an

administrative nature and responsibility for the professional aspects of practice in the office. I also had a number -- during the period that I returned, over the months right after my return to Washington as a partner, we did, so to speak, reshuffle some client engagements among the partners -- there were two then -- and I did have various clients as client partner, engagement partner, if you will.

Q Approximately how many clients would you have had as engagement partner, sir?

A I think at that time I probably had somewhere between 15 and 20, some such number.

Q Did there come a time, sir, when you first heard of the National Student Marketing Corporation?

A Yes, there did.

Q When did you first hear of National Student Marketing Corporation?

A I first learned of the company NationalStudent Marketing in a telephone conversation from Larry Hoerner, who was a partner in our Kansas City office of the firm.

Q What did Mr. Hoerner say to you in that conversation and what did yousay to him?

A Larry Hoerner told me that he had been contacted by a gentleman named Cortes Randall, and here I am referring to the son, who we have been calling here in court the president

of National Student Marketing. He apparently had met Mr. Randall over the preceding weeks or months. I don't recall which.

Mr. Randall had contacted him to inquire about his interest in Peat, Marwick possibly becoming the auditors for National Student Marketing Corporation and Larry's purpose in calling me was to set up a meeting in Washington so that he and I could meet with Mr. Randall in Washington, where National Student Marketing's offices were located at the time.

Q Did there come a time when you had such a meeting?

A Yes, there did.

Q Who was present at that meeting as best you can recall, sir?

A As best I can recall, for most of the meeting, Mr. Randall, the president, Larry Hoerner and I were present. I am not sure if Randall, Sr. was present at that meeting or not. He may have been. At some point during the meeting my recollection is that Bernie Kurek was brought in and introduced to us as the relatively recently engaged comptroller of the company.

Q Would you tell us what was said at that meeting, as best you can recall. First, where did this meeting take place?

A In Mr. Randall's office inWashington, D.C.

Q Can you give us an approximate date for that meeting, sir?

A Roughly the third week of -- some time in the third week of August. I believe it was on a Friday, if I recall correctly.

Q What do you recall being said at that meeting?

A Well, it was -- I would call it kind of a typical first meeting with a prospective client, where Mr. Randall described to us what his company, National Student Marketing, was about, he described to us the background of the company, how he had founded it himself several years prior, that it was a rapidly-growing company, that it had some time earlier that year merged with another company and had had a public registration of its stock.

He described the fact that the major emphasis of this company, National Student Marketing, was directed towards providing services for national-type companies, major companies in the United States, in the area of providing services to the youth market, that is, providing services whereby these national companies could reach the youth market with announcements about their products or services, to identify with the youth market.

On the other hand, from our standpoint, that is,

Peat, Marwick's standpoint, we gave Mr. Randall some idea of how Peat,Marwick, Mitchell was organized and what my position was, Mr. Hoerner's position was, the number of offices in the firm,and so on. A typical kind of meeting.

Q Was there any discussion at that meeting as to where National Student Marketing Corporation would maintain its offices?

A Yes, there was. Mr.Randall indicated that the company had planned -- he had planned to move within a relatively short period of time. If I recall correctly, the framework given was some time no later than the next couple of years, but I can't recall that precisely. The company did plan to move its offices to New York City because they apparently recognized that that is where most of the major activities that they would be involved in would kind of be centralized.

The reason for the offices being in Washington at that time were essentially that Mr. Randall, and his family, as I understood it, was from that area, and hence set up the office near home when the company first was founded.

Q Subsequent to this meeting did you have occasion to attend a meeting in New York City?

A Yes. Shortly after that initial meeting -- it may have been the following week; I think it was the following week -- we were invited to attend a meeting at the then New York City offices of National Student Marketing Corporation.

Q Who was present at that meeting?

A There were a number of people present. I really can't remember all the people that were there.

Maybe I can describe what the purpose of the meeting was. That might give some answer to your question.

Q Why don't you tell us who was present, if you recall, from Peat, Marwick, Mitchell?

A From Peat, Marwick, Mitchell I do recall that Joe Scansaroli, who I had selected as the proposed supervisor for that engagement, was with me, I was there, George Terry, the tax partner in our Washington office was there, so that he could gain some knowledge about this new client, to the extent that he would be involved in tax consultation with the company, and in addition I had arranged, because the company was planning to move to New York, I had arranged for a partner from our New York office to attend that meeting and it was someone in New York-- I forget who I contacted, but someone assigned -- Art Phillips, who was a partner in our New York office -- to attend the meeting for that purpose,

so that we would have some knowledge in our New York office looking toward the transition at some point of the client from Washington to New York.

Q As Peat, Marwick is structured, if a client moved to New York what responsibility wouldyou maintain in regard to that client?

A Well, the way Peat, Marwick is organized, we have -- well, I don't know how many offices we had at that time. We have approximately 107 offices now in the United States.

Our practice, our policy is to have the office in which a client's corporate headquarters or at least -- there should be a distinction. It is usually the executive offices dealing with the financial activities of the client. The office inwhich that geographic area the company is located would be the so-called client office. So at such time as NSM would move to New York my responsibilities as a client partner would cease and some partner in the New York office would become the client partner for that organization.

Now, if there was any additional work to be done in Washington, if they had operations in Washington, in all likelihood I would have performed whatever services New York would request the Washington offices to perform

in helping them to complete any work.

Q You told us who was at the meeting in New York from Peat, Marwick, Mitchell's side. Who was there from National Student Marketing's side?

A Well, I know that Cort Randall was there, I believe Bernard Kurek was there. Mr. Randall, Sr., I can recall being at that meeting, and there were quite a number of officers of National Student Marketing, department heads of National Student Marketing, people involved in various aspects of National Student Marketing's business, and there were other guests at that meeting being officers, as I recall, of a proposed acquisition, a company that had been talking to National Student Marketing about possibly merging together. This particular one, as I recall, never did become a merger candidate, but it was a company from Salt Lake City.

I remember that. It was involved in educational programs for students in Europe during the summer.

Q What was the nature of the discussion that took place? Tell us the substance of what occurred at that meeting?

A The purpose of the meeting that we attended and the reason that we thought it would be a good idea to attend at that point is that National Student Marketing personnel, people from the various departments in National Student Marketing, were telling, in essence -- telling the people that they were interested in possibly merging with, what National Student Marketing was all about, the manner in which they reached the student market essentially at the college level and to some degree the high school level through their network of student representatives, so-called campus representatives, and through various programs of being able to mail directly to students at either their home or student -- excuse me, campus locations based on mailing lists that they had available and that was -- part of that was ~~shaver representatives~~ Schaffer Enterprises, and that was how Larry Hoerner first became involved.

We represent in Kansas City ~~shaver enterprises~~ Schaffer Enterprises. That was the purpose, to let these possible acquisition candidates, the officers of the company, know what National Student Marketing was about.

Since we were becoming involved in the company

at that time, with the company as their auditors, it was an opportunity to gain some feel of what the company was about.

Q Mr. Natelli, would you try again to speak up a little louder and speak a little more slowly.

A Yes.

Q Did Peat, Marwick, Mitchell become the auditors for National Student Marketing?

A Yes, we did.

Q At the time that you became auditor for National Student Marketing, in any of your discussions with Mr.Randall did you discuss a question of who had been the prior auditors and any reasonthat that relationship had terminated?

A Yes. I guess I should have mentioned that before in the question you asked me. At the initial meeting with Mr. Randall that Larry Hoerner and I had, we did ask Mr. Randall, as would be customary, who had been doing the work, and I believe Larry Hoerner may have actually known this before, before we arrived at the office. We knew that another firm, Arthur Andersen & Company, had been the auditors of National Student Marketing and we asked Mr.Randall why it was that he was interested in making a change from one accounting firm to another.

Q What did Mr.Randall say on this subject?

A My best recollection was that he was essentially discontent because during the previous year or more that there had been association withArthur Andersen, the fees that they were charging continually resulted in amounts that were considerably in excess of what they had estimated the fees would be.

That was the essential reason.

I do recall that we asked him if there were any disagreements with Arthur Andersen, any professional areas, and he answered that there were none.

We also, of course, asked or we also told him that it would be necessary for us in due course to contact Arthur Andersen to make such inquiry ourselves and had to obtain his permission to do that, which he did give us.

MR. MARTIN: Can we mark as Natelli Exhibits S and T these two documents.

xxx (Defendant Natelli Exhibits S and T were marked for identification.)

Q I show you, sir, what has been marked as your Exhibits S andT for identification, and askyou if you would tell the ladies and gentlemen of thejury what those two documents are, without describing the contents thereof?

A Exhibit S is a letter addressed to Mr. Everett Parkinson, a partner at Arthur Andersen & Company in Washington, dated September 5,1968, sent by me, if I didn't already say that.

Exhibit T is a letter fromMr. Parkinson to me, dated September 9, 1968.

MR. MARTIN: Your Honor, at this time I would offer Natelli Exhibits S and T for identification into evidence.

THE COURT: Is there any objection?

MR. VELIE: No objection.

xxx (Defendant Natelli Exhibits S andT for identification were received in evidence.)

MR.MARTIN: May I read these to thejury, your Honor?

THE COURT: Sure.

(Mr. Martin read from Natelli Exhibits S & T in evidence to thejury.)

Q Is it true then, sir, that in September Peat, Marwick & Mitchell was the auditor for National Student Marketing Corporation?

A Yes, sir.

Q And when did the work in preparing for that audit begin, as best you can recall?

A It was right around the end of the fiscal year of the company, which was August 31,1968. I believe it may have commenced right before that time, either right before or right after that.

Q When you first became the auditors for National Student Marketing Corporation, sir, were there any matters relating to that company that were brought to your attention?

Let me withdraw that for a minute.

Who was assigned to conduct the audit of National Student MarketingCorporation for Peat, Marwick, Mitchell?

A Well, of course I was the client partner myself, the engagement partner.

In addition, Joe Scansaroli was assigned as the supervisor on the engagement, John Johnston was assigned for at least some period of time as senior on the engagement and Doug Oberlander was assigned as the assistant accountant on the engagement.

Q Would you tellthe ladies and gentlemen of the jury, Mr. Natelli, the type of responsibility that a partner has with regard to an audit engagement?

A Well, a partner has the,so to speak, full responsibility of the firmwith respect to an audit engagement. He is the individual who has the responsibility to maintain the relationships with the client with respect to whatever

services might be needed, be they tax or audit. He would have the responsibility of assigning people for the various services to the client.

He would also meet with the member of management and to some degree as appropriate members of the staff under the supervisor manager in order to discuss matters that come up during the engagement of a nature that require his decision.

In essence, he has the authority to make whatever decisions are necessary from a policy standpoint in conducting the work for the client.

Q Does the partner generally get involved in the detailed review of the client's books and records?

A No, I wouldsay usually a partner does not.

Q WhenPeat, Marwick, Mitchell became the auditors of National Student Marketing, were there certain problems that were brought to your attention as the partner in charge of that engagement?

A Well, it is a fairly broad question.

My recollection is that the matters that I can recall as being of significance was, of course, the fact that we did have a situation where the company was relatively new, in existence a few years, but in terms of administrative area had a newly engaged comptroller who

was in the process of getting things straightened out administratively, had been there working on that since he arrived in June.

So this ~~naturally~~ naturally created a situation which required certain approaches with respect to how and when you get involved in doing audit work.

It also was -- there also were some acquisitions, as I recall, in process at the time or contemplated, so there were immediately during that initialperiod some questions of how to account for acquisitions that came up during the initial month or two.

For some time during that period of time during the audit what, of course, is the major item of consideration which had to be given from an accounting standpoint is the fact that there were fixed fee-type business arrangements by the company which had to be considered by me in order to arrive at a decision as to how this matter should be accounted for and audited.

End 2

Q When did the question of the fixed fee contracts first come to your attention as best you can recall, sir?

A My recollection is that it was either the end of September or the beginning of October, somewhere in that time frame.

Q How was this matter brought to your attention?

A My best recolledtion is that Joe Scansaroli brought it to my attention. I can't really recall how, whether he met with me or telephoned me or what. But Joe advised me that he had been in discussions with Cort Randall and Bernie Kurek about this area of the company's activity and he felt that I should join a meeting with them in order to discuss this aspect.

Q Did you have a meeting with Mr.Scansaroli and representatives of National Student MarketingCorporation?

A Yes, I did.

Q Where,as you recall, did that meeting take place?

A My recollection is that it took place at the offices of National Student Marketing in Washington. I can't recall specifically whetrher it was Bernie Kurek's office or Cort Randall's, but one of the offices there.

Q Who was in attendance at that meeting?

A I recall Cort Randall, Bernie Kurek, Joe

Scansaroli and me being at that meeting. I don't recall that there were others, although there may have been.

Q Approximately when did this meeting take place?

A Either the end of September or beginning of October, somewhere in that time frame.

Q Do you recall what was said at that meeting? Would you tell us the substance of what was said as best you can now recall it, what Mr. Randall said, what Mr. Kurek said, what you said and what Mr.Scansaroli said?

A My best recollection is that the meeting was mostly conversation between Cort Randall and me with from time to time perhaps comments or observations being made by Bernie Kurek and Joe Scansaroli. But it was essentially a meeting in which Cort Randall was describing to us this area of activity called fixed fee type business.

Q Would you tell us what Mr. Randall said about this subject?

A Well, Mr. Randall described to us this fixed fee type business as being an area of activity that the company had gotten into substantially during that fiscal year. He spent a considerable amount of time explaining to us what was involved in this activity, distinguishing it from the so-called per inquiry type of activity in which the company had been engaged ever since its foundation and really

ever since -- that was the way in which the company got started, the per inquiry type.

Q Would you tell the ladies and gentlemen what he said about these subjects and the distinctions that he made?

A Well, as best I can recall, the suggestion was this: The per inquiry-type business, based upon which the company was founded, was an activity where the company through various means, either by sending out mailings to students or by having campus representatives place on campuses posters of various types, would be designed to obtain from the students some response. Hence the reason they called it PI or per inquiry type business.

Now, the response from the students would represent either their actually sending in money with some particular order form to buy a product, let's say an alka-selzter plastic air-fillable pillow for their bedroom, that kindof thing -- this is one of the type products -- or a subscription for a magazine, Time Magazine, for example, being one of the major clients of National Student Marketing at that time, or just a questionnaire type thing, where a company might be interested in determining how students would react to certain types of programs and the questionnaire would be completed, sent in by the students.

Now, this per inquiry type business or in this per inquiry type business National Student Marketing would be paid by their clients based on the responses from the students.

So for example for a magazine subscription, the way they got paid for that is the subscription would go to Time Magazine -- I might be wrong; it might go to NSM and then Time -- but whatever, based on the subscription to Time Magazine, National Student Marketing would get some portion or perhaps all of the first year's subscription. I don't recall all the amounts, but they would get paid based on what the students' response was, either to a product, a questionnaire, to a service.

He explained that as distinct fromthat type of business that the company had become heavily involved in during the year about which we were speaking was this fixed fee type business.

Now, the contrast between the two is that in fixed fee type activity the account execs who had been brought into National Student Marketing during that year were in essence consultants, consultants to companies, consultants to companies like American Airlines, various large companies in the country, and their purpose or their business was to consult with these companies, develop or

help them develop ideas as to how they could reach the student market which National Student Marketing felt it was very knowledgeable about. Their activity was described as essentially being creative efforts in this whole field of reaching the youth market, as a result of which a client would commit to National Student Marketing to carry out certain programs of advertising methods either by mail or, once again, using the extensive campus rep system that had already been developed and in existence for some years, but it would be done at some agreed figure, some price.

In other words, whether or not a student response was involved had no part to play, as we understood it, in this type business. It was based on the service, the ingenuity of the account exec in working with the client to get them to see how National Student Marketing could be of help to them, and going ahead with a program.

Q Was there any discussion by Mr. Randall as to how the company had accounted for this in the current year or how the company felt this should be accounted for?

A My recollection is that Mr. Randall suggested, recommended, however we may wish to put it, that this income -- that these commitments, the income from these commitments, be accounted for on the basis of the time that the account

executive received a commitment from his client, and he also indicated to us during the course of that discussion that this is the way that the company had accounted for this income in the nine months statement that had been submitted to its shareholders as of May 31, 1968.

THE COURT: Mr. Martin, I apologize for interrupting, but would you tolerate an interruption here. I have some other matters that have come up here that I have got to handle. Is that all right?

MR. MARTIN: Certainly.

THE COURT: Forgive me, ladies and gentlemen of the jury. We will take a recess at this point and I will take care of what I have to do and be back shortly.

(Recess.)

THE COURT: All right, Mr. Martin.

BY MR. MARTIN:

Q Mr.Natelli, just before we broke you were telling us about a conversation with Mr.Randall concerning his views as to how this income on these fixed fee contracts should be recorded and how it had been recorded. Did you tell us what he said on those subjects?

A My recollection is that he was recommending that the contracts be recorded the same as they had been in the company's May figures, which as I recall was to

record the total amount of profit on the contracts, in other words, 100 per cent of whatever the commitment gross profit was.

Q When would this 100 per cent be recorded, what would be the date that would determine the recording of the income?

A My recollection is that it was the date as of which a client committed to an account executive that they were going to use NSMC services.

Q Did you reach any decision at this meeting as to whether or not you would approve this as an appropriate method for the company to report its income?

A No,we did not, I did not.

Q Did you and Mr.Scansaroli have any discussion at this meeting? Did you say anything in response to what Mr.Randall had stated?

A Well, as best I can recall, there was some preliminary discussion of what the alternatives might be to record this type of business, to account for it.

Q Did you reach a decision?

A No.

Q Did you and Mr.Scansaroli have any opportunity, either at that meeting or separately, to discuss among yourselves, between yourselves, whether this was an

appropriate method for the company to record its income?

A I think I may have turned to Joe during that meeting or toward the end of it and asked him if he had any particular feeling about it and he indicated that he didn't, that it was up to me to give the consideration, and really we had no -- I had no intention of arriving at a decision [redacted] at that meeting, so we had subsequent discussions about it.

Q Do you recall what Mr.Scansaroli said in that regard,sir?

A Well, if I recall,Joe made a typical comment like "Well, I don't get paid to make those kinds of decisions.'

Q You were the partner, I take it?

A Right.

Q And he was the supervisor?

A Right.

Q And the decision was whose, sir?

A It was mine.

Q Did you, after that meeting, have occasion to discuss this further with Mr.Scansaroli?

A Yes. There was some point after that initial meeting when Joe and I had additional discussions about the ~~whole~~ whole topic, fixed fee type business.

Q Where did those discussions take place as best

you can recall?

A The best I can recall, they were in my office in Washington.

Q Would you tell the ladies and gentlemen of the jury the substance of that discussion between you and Mr.Scansaroli.

THE COURT: First of all, let's be sure of something. Was there just one discussion or did you say, which I thought you did, there were a number that you and Scansaroli had?

THE WITNESS: Your Honor, I can't be definitive about that. My best recollection is that we probably had a couple of conversations. Joe was in and out of the office on various matters. There was then one meeting at which some tentative conclusions were reached.

THE COURT: I see.

I take it, again, since I have interrupted already, that this was some time in early October still?

THE WITNESS: Yes, sir.

THE COURT: Thank you.

Q Can you distinguish between the discussions that you have mentioned to his Honor?

A You mean can I actually place various conversations?

Q That's right. Can you distinguish what happened at one from what may have happened at another?

A I know, for example, that we had to -- at the meeting that we spoke of previously, I am sure that one of the things -- when we left that meeting what happened was the company was to accumulate the information about this particular type of activity which it had not yet accounted for on its books. There may have been some discussion between Joe and me beyond that as to how the company was doing and other information.

I really can't. I can't draw any distinction between -- I can't recall specific meetings that we may have had during that period of time.

Q Can you recall the substance of the discussions that you had with Mr. Scansaroli in these meetings that took place subsequentto the time you had this meeting at which Mr. Randall and Mr.Kurek brought this fixed fee problem to your attention?

A Yes. Essentially we were discussing the fact that we did have to account for this type business in some way and we discussed the alternatives that might have been possible to account for this type of activity. There was some discussion also at some point in there as to the audit aspects, the audit problems that might be involved.

Q Take one thing at a time. What were the alternatives that were discussed?

MR. VELIE: Your Honor, may we have who said what to whom here rather thanthe subject matter?

Objection as to form.

THE COURT: I am not sure that the form of the question is faulty. On the other hand, I agree with you, and I assume Mr. Martin agrees with you, if we can get it.

Q The best you can recall, would you try and give us what you said and what Mr.Scansaroli said?

A It is pretty difficult to remember which accountant said what in the course of a discussion about these kinds of matters, frankly.

Well, maybe the best -- well, I can recall that what we were discussing pertained to how we might account for this business. I think that I came up with several alternatives that we might consider and kind of bounce them off of Joe Scansaroli, if you will, as to what he thought of them, and from what he knew about the records of the company, how they might fit in the whole decision process.

We discussed -- I suggested, for example, that one approach might be to consider deferring the costs of this account exec fixed fee type program as of August 31, 1968, and trying to amortize -- allocate these costs and then amortize them over the fixed fee type contracts as they were eventually fully serviced, so to speak, with whatever third party services might be involved.

That was one approach that we kicked around. I think on that particular one we concluded that it would not be something that we could do, although from an accounting standpoint it was a perfectly acceptable alternative in this situation. The company was doing a great deal of building up of its services in its New York office and the various expenses which would be involved here that

would have to be allocable, if you will, and deferred, such as the costs of rents, secretarial services, travel, whatever else they were, I don't really remember, that we had talked about.

The records were such that it would be difficult and the nature of services was such it would be difficult to distinguish between the various types of revenue services to the company that were forthcoming from these costs.

It was difficult to arrive at that approach.

One other approach that I suggested we could consider would be the so-called completed contract method where, in essence, you would not record any gross profit on any of these commitments until the ultimate future point in time when all of the services required to be provided, including the third party type items of putting posters up and mailing and so on, would be completed in toto, and at that point there would be a determination of the gross profit for recording at that time.

Of course, there was the method that Mr. Randall suggested, which we also did consider, and that method, as I described, was to take all of the gross profit in at the time of the commitment, and the other method that I suggested, that might be appropriate here in my reviewing it, was the so-called percentage completion method.

I discussed this with Joe as well.

Q Did you have any discussion about the audit procedures which would be followed with respect to these contracts? Did you reach any tentative conclusion at this meeting as to what method would be adopted?

A Yes. At a particular meeting which I am referring to the substance of these matters was being discussed.

I reached a tentative decision based on my conversation with Joe that we would pursue the percentage of completion type accounting for this fixed fee type activity.

Q Were there discussions at this same meeting as to the audit procedures that would be followed?

A Yes, there were.

Q What were those discussions, sir? Again if you can try and separate who said what it would be helpful, although I know it is difficult.

A It was certainly on our minds that one of the problems that we had to face was the fact that the company was behind in terms of gaining control over its administrative activities. So naturally irrespective of which method that we chose, this was a matter that we had under consideration.

My best recollection of what we had tentatively

concluded with respect to the audit aspects was that Joe would visit with the account execs who were after all involved in this activity, meet with them or a selection of them at his choosing to discuss the commitments that they had, the type of business that they had from these clients, would review their files to the extent available to determine if whatever paper work might be involved concerning business meetings and so on would help to substantiate what had taken place, and since at some point in time here, and I c-an't recall exactly when, but I think some time between the initial meeting about which we spoke previously with Mr. Randall and Mr. Kurek, some time between then and our tentative conclusion meeting, if you will, we were made aware that because these commitments were oral, the client had asked if there was some means other than written confirmation by which we would confirm with the client of NSM that these commitments existed.

That was a consideration, and my conclusion on that particular aspect of this whole problem was to instruct Joe that he should make telephone calls on a selected basis at random, so to speak, with or to the clients who were the clients of NFM on these commitments.

Q Did there come a time when Mr.Scansaroli did go to New York to carry out this audit work that you and he

had discussed?

A Yes, there did.

Q Do you recall approximately when that was?

A I know it was some time in October.

Q Did Mr.Scansaroli report back to you on the work that he did?

A Yes, he did.

Q Where did that meeting take place, as best you can recall?

A I believe it was also in my office.

Q When approximately was that?

A I would guess the end of October.

Q Again, was anybody else present?

A Not that I can recall.

Q Can you tell us what the substance of the conversation was that you had with Mr.Scansaroli on that occasion, what you said to him, what he said to you, as best you can recall?

A Essentially I asked Joe what the findings of his trip to New York were, and he described to me briefly that he had performed the procedures which I had instructed him to, he had met with account execs, had reviewed their files and had made telephone cdalls.

Q Did you at this meeting reach any conclusion as to whether or not it would be appropriate in light of everything you knew at that time for the company to record income on these contracts on a percentage of completion basis?

A Yes. I arrived at a conclusion after speaking to Joe that we would account for this fixed fee type activity on a percentage of completion type basis.

MR. MARTIN: May I have Exhibits 3 and 5, Mr. Velie?

(Pause.)

Q I place before you, Mr. Natelli, Government Exhibit 3 in evidence, which is the special sales work binder, is that correct?

A Yes, sir.

Q Did you have occasion to review that document after it was prepared, sir?

A I think I may have reviewed it at a time when it was not yet complete, probably in the course of my discussions with Joe Scansaroli with the work he had done. It wouldnot have been a review in detail, as I recall, but kind of browsing at pages that represented his notations of some tracts of what work he had done.

Q The decision that was made, sir, to permit the

company to record the income on this basis, was that your decision?

A Absolutely.

Q Was that your responsibility as a partner in charge of that engagement to make that decision?

A Yes, it was.

Q Was it Joe Scansaroli's responsibility to make that decision, sir?

A No, sir.

Q Were you aware at the time, sir, that you made that decision that the decision might mean the difference between a profit and a loss to National Student Marketing Corporation?

A I amnot sure that I was aware that it would represent a difference between the profit or loss to the company, but I certainly knew that it was a significant matter, and the results of that decision would have some significant effect on the company's reported earnings, yes.

Q I show you Government Exhibit 5, Page 16. That document reflects unbilled receivables and accrued cost and estimated earnings on contracts in progress, Note 3, and the figure $1,639,992.

Who was it, sir, that determined that that

title should be used for that asset account?

A I made that determination.

Q Note 3 referred to therein reads: "Contracts in progress." Who drafted that note, sir?

A I did.

Q In drafting that note did you try and distribute the situation as you understood it with regard to the theory on which National Student Marketing was booking income on these commitments?

A I did, sir.

Q Will you turn, sir, to the page where the auditor's report appears in that document.

Do you have that, sir?

A Yes.

Q Is the name Peat, Marwick, Mitchell in script photocopied in that document?

A Yes, it is.

Q Is that a reproduction of an actual signed document signed on behalf of Peat, Marwick, Mitchell & Company?

A Yes, it is.

Q Who signed that document?

A I did.

Q You recall that there has been reference to the special sales binder.

MR. MARTIN: I would like to read a portion of Mr.Scansaroli's writeup of October 26 at this time, if I may, your Honor.

(Mr. Martin read from Government Exhibit 3 in evidence to the jury.)

Q Mr. Natelli, would you tell the ladies and gentlemen of the jury to whom the auditor's report that you signed is addressed?

A The board of directors and stockholders,

National Student Marketing Corp-ration.

Q Does that report that you signed bear a date, sir?

A Yes,it does.

Q What is the date of that report?

A November 14, 1968.

Q Was that the date that the financial statements were actually issued, sir?

A No. They in all probability were issued some time later than that date.

Q What does the date represent as far as the auditor's report is concerned?

A The dating of the auditor's report represents the date as of which what we would refer to as field work is substantially completed. This is the time at which most of the work which involves being at the client's office is completed and hence a date which signifies the completion of the substantial portion of the work.

Q Directing your attention, sir, to early December 1968, did you have occasion to have a meeting with representatives of National Student Marketing Corporation?

A Yes.

Q Can you fix the approximate date of that meeting, sir?

A There was a meeting somewhere near the beginning of December. Through looking at some documents recently in preparation for this trial, it was I think December 8 or 9, something like that.

Q Who attended that meeting as best you can recall?

A I can specifically recall Bernard Kurek, Cortes Randall, Joe Scansaroli and I being present. I seem to have a hazy recollection there may have been other individuals in the room during the meeting, but I am not sure who they were.

Q Do you recall whether or not John Buck was present?

A I am not sure, but he may have been.

Q Where did this meeting take place?

A At National Student Marketing's offices, either Mr. Kurek's or Mr. Randall's office. I am not sure which.

Q Will you tell us, sir, what was said at that meeting by the various people, and as best you can recall, give us the substance of that meeting, what the various people said.

A Well, my recollection of that meeting is that it was what we refer to as a sort of exit interview. It was a meeting at which we meet with the client and discuss matters that have come to our attention during the course

of the audit, which had fairly recently been completed, and discuss with them our recommendations as to what corrections or improvements we suggest are necessary, and at this particular meeting certainly the emphasis of the meeting that I can recall is that I discussed with the client the fact that while we had faced the situation and dealt with it when we came into do the audit as of 8/31/68, with respect to their accounting and so on, especially in this area of fixed fee contracts, recognizing that they were in the process of trying to get things straightened out, cleaned up, and so on, and we had to deal with the situation as it then existed, most of our recommendations dealt with their getting under administrative control their various accounting matters.

In particular, I know that one of the important elements of that meeting was the recommendation on a prospective basis from that point forward to record commitments on this fixed fee type business on the basis of a written commitment.

Q Was there any --

A Excuse me. Which brings to mind, I do know because of what occurred there was one other individual present -- that was John Davies -- at that meeting.

Q Was there any discussion of the confirmation

procedures that Peat, Marwick, Mitchell would use for the audit the following year, 8/31/69?

A Yes. In connection with the discussion that I had, saying "Look, you know, we dealt with what we found here and dealt with it appropriately, as we considered," it was made clear to NSMC that with respect to the following year 8/31/69 audit that we would expect them to be in a position where we could send written confirmations on this fixed fee type business.

Q Was there any discussion at this meeting about any other records that National Student Marketing Corporation should maintain with regard to these contracts?

A Yes. In the sense of discussing the administrative matters which had to be improved in this area, we recommended to the client that time logs be established so that the account executives would report on a periodic basis -- I don't recall it was weekly or bi-weekly -- but a periodic basis, record their time that they were spending on the various client commitments, and submit these to the accounting department so the accounting department could maintain records of time by account executive by client contract.

Q Do you recall anything else about that meeting, sir?

A I think there were some other forms discussed along that nature, including a status report, which -- I forget the frequency -- but once again, a status report by which the account exec would indicate to the accounting department his then current estimate of what his percentage of completion was on a particular contract.

Q I show you, sir, your Exhibit G. Would you tell us please what that is.

A This is a form of program commitment letter which was the result of the meeting that we just discussed. My best recollection is that it was drafted by John Davies, who was then an outside counsel, legal counsel, to the company. He drafted it. I may have made some changes from some original draft. I really can't recall. But it was basically his drafting a form of letter which from his standpoint as an attorney he advised me he considered would be an appropriate binding contract in written form and from my standpoint as an accountant I agreed that it served our purpose in seeing to it that the company was improving its administrative practice in this area.

Q When was that letter prepared as best you can recall?

A My best recollection, sir, is that it was a

few days after that meeting that was discussed.

Q Directing your attention, sir, to the period from December to early May of 1969, did you have any contact with National Student Marketing Corporation or any of its officers or agents during that period?

A Yes, certainly.

Q Can you briefly, sir, tell the ladies and gentlemen of the jury what the nature of your involvement with National Student Marketing Corporation was during this period from late December to let's say the end of April 1969, late December 1968 to the end of April 1969?

A My essential involvement at that time -- the audit for '68 at that point was something that was behind us, was history -- my essential involvement was with respect to various mergers that the company was considering, either that they had actually gotten involved in or were considering as prospective mergers, discussing with them matters of accounting treatment which should be accorded to these mergers. That I would say took up most of whatever involvement I had with the company at that time.

Q What were the matters of accounting treatment that you were discussing, sir?

A Well, I would typically receive a phone call from Jim Joy, who was I believe a member of the board and

a partner in the company's investment banking firm, or Mike Matthews at the law firm of White & Case, which was the company;s outside counsel, or perhaps sometimes John Davies, where they would tell me about a prospective or a definite merger candidate that they had and would ask me what the accounting treatment would be that would have to be afforded to the transaction if it went through as was being contemplated in terms of what the exchange of shares or notes or cash was between the party. Essentially this involved the distinction between what is called purchase accounting and pooling of interests accounting and it was a very problematic area during that time, and phone calls would come in fairly frequently to discuss these matters.

Q During this period, sir, did you have -- again we are talking about December '68 through late April '69 -- did you have any occasion to discuss the fixed fee contracts with anybody associated with National Student Marketing Corporation?

A Some time during that period, I believe in the month of April, I was advised as to certain writeoffs that the company was going to have to make with respect to these contracts,yes.

Q Prior to that time in April when this question of the contract writeoffs came up, before that, going back

to December, had you in the intervening period had any discussion about these contracts with anyone associated with National Student Marketing as best you can recall?

A I am not sure I understand the question.

Q Just simply from the period late December 1968 --

A Right.

Q -- until you first heard in late April, I think you said, of the need to write off certain contracts, had you had any discussions about these contracts or the methods that the company was using in relation to these contracts with anybody at National Student Marketing Corporation?

A Well, no specific or significant discussions other than from time to time if I would see Bernie Kurek I would ask how things were going in the company's getting the administrative matters under control.

Q I show you what is marked Government Exhibit 10A in evidence, which you will recall is a document that Mr. Kurek identified during his testimony and said that it was a document that he gave to you, he believed, some time in March 1969.

Do you recall receiving that document from Mr. Kurek?

A No, sir, I can't recall having seen this document prior to the coming up in the course of the trial here,

trial preparation.

Q Can you say definitely whether or not you have ever seen it before?

A I would be hard put to make a statement that I never saw it. I don't recall seeing it.

Q You will recall Mr. Kurek also testified about a meeting he had with you in March of 1968 attended by you, Mr. Kurek and Mr. Randall -- I believe he said he thought it was a Saturday meeting -- at which there was some discussion about the contracts of NationalStudent Marketing. Do you recall that testimony?

A Yes, I do.

Q Do you recall attending such a meeting?

A I am sure that I may have attended some meeting on a Saturday with Mr.Randall and Mr. Kurek, but I cannot recall any discussion about the contracts in the way that Mr. Kurek has testified here, no.

Q You started to tell us before about an event in late April when it was brought to your attention that certain contracts would have to be written off. When did this occur, sir, and how did this matter first come to your attention?

A My best recollection, it was some time in April that in the course of a telephone conversation I believe

with John Davies, or it may have been Cort Randall, but my best recollection is that it was probably a phone call with JohnDavies in which he advised me about the fact that -- I can't think of the individual's name now -- Ron Michaels -- Ron Michaels, who was an account exec of National Student Marketing, had been discharged by the company, the reason for his discharge was because of unethical conduct, and that the company had learned he was taking kickbacks from certain suppliers of the company, and consequently he was discharged.

He advised me that as a result of that there were some changes in client responsibilities and that in this connection it was learned that his contracts were no good, they were never commitments in fact.

I can't recall precisely why I was having this phone conversation with John Davies -- it was a call that I believe he made to me -- but I am pretty sure that it was in the course of that phone conversation that this was discussed.

As a result of this I spoke to Cort Randall, because it did concern me, of course, to hear this. I may be mixed up in the order of whether Cort Randall told me first and then I spoke to John Davies to, you know, confirm from one to the other and get more details, but my

best recollection is I spoke to Davies and then I spoke to Cort Randall on the phone when I found out about it and confirmed the information I had received in the first telephone call, and it was my understanding that as a result of Ron Michaels being discharged some other account execs had been assigned to his contracts and in the course of pursuing these client contacts it was discovered that client commitments never in fact existed insofar as the clients were concerned.

Q In the course of these conversations with Mr. Davies and Mr.Randall did they suggest to you, sir, how these writeoffs should be made on the books of National Student Marketing Corporation?

A No, they did not.

Q Was a decision made as to the method for writing off these contracts on the books and records of National Student Marketing Corporation?

A Yes, there was.

Q Who made that -ecision?

A I did.

Q Did you discuss that decision with anyone else before you made it?

A I am quite sure I discussed the matter with Joe Scansaroli to advise him of it. It may have been in the

course of other discussions, but I would think that it was an important enough matter that I probably mentioned it to Joe when it did happen. That may have been before or after I had already decided. I am not sure.

I do recall telephoning Bernie Kurek to find out if he knew about the Ron Michaels situation, since he had not mentioned it to me, and I remember when I phoned Bernie Kurek he said no, he didn't, he was not aware of the fact that this situation had developed and the contracts had to be written off, and I told him what I had learned and suggested that he find out about it and that I was giving consideration to it, and I think at that point I had reached a tentative conclusion that it would have to be written off retroactively.

That is my recollection of who in the way of individuals I discussed this with once I had gotten to or was making my decision.

Q Did Mr. Kurek suggest to you how these contracts should be written off?

A No, sir.

Q What was your decision with regard to how these contracts should be written off on the books of National Student Marketing Corporation?

A What was my decision?

Q Yes.

A That they be written off retroactively to August 31, 1968.

Q What was the basis of your decision?

A The basis of my decision was my consideration of the fact that the booking of these contracts in August 31, 1968, was based on an understanding that there was a client commitment to National Student Marketing to use certain services.

I was now being told by the client that it turned out that this commitment apparently never existed, and consequently, had we known at the time about Ron Michaels and his apparently not having had these commitments, then we would not have reported it in the first place, and it was my decision that in view of that this represented what in essence would be a prior period correction and the retroactive adjustment was necessary.

Q That was your decision?

A That was my decision.

Q It was not Joe Scansaroli's decision?

A No, it was not.

Q Directing your attention to approximately the same period, late April, early May, did you have any occasion to discuss with anyone the question concerning the provision

for deferred taxes that was set forth in the original report you had issued with respect to the financial statements of National Student Marketing, which is now contained in Government Exhibit 5?

A Yes, sir.

Q Would you tell us, sir, with whom you had these discussions as best you can recall?

A My best recollection is that Joe Scansaroli brought to my attention that Carol Raimondo had in the course of preparing the tax return of the company for the year ended August 31, 1968, determined that in her opinion we had incorrectly provided in the accounting statements for deferred taxes and that Joe and she had had some discussion of this, and had concluded that that was a fact.

Q Any other discussdon that you had with anyone else?

A Well, obviously when I heard about it, it was a matter of concern, and I got together the parties who would have been involved in such a matter, Joe and Gene Holloway, the partner in charge of our tax department, and I would have thought that Carol Raimondo also may have been at this meeting. I know there was a meeting in my office shortly thereafter. I was advised about it, whatever time it took to get together on it.

The matter was discussed and, if I recall, it was Gene Holloway who advised me that,yes, he was made aware of this by Carol and had looked at it and concurred in the decision.

So it was, after I heard about it and heard the discussion, I understood what they were telling me, and I agreed with what they said.

THE COURT: You are looking at Government Exhibit 5, right?

THE WITNESS: Yes.

THE COURT: What page are you looking at?

THE WITNESS: I just happened to be looking at Page 18, sir.

THE COURT: Is that because there is some

figure there that refreshes your recollection and, if so, I am curious to know what is that figure?

THE WITNESS: No, there is no figure here that happens to refresh my recollection. I am looking at it because counsel asked me to look at it.

THE COURT: I agree withyou. I was puzzled as to why he asked you to look at this in this context.

MR.MARTIN: Let me see if I can clarify that.

THE COURT: And also are you telling us that you heard this from Scansaroli in May of 1969?

THE WITNESS: It was April or May, sir, in that time frame.

THE COURT: You would agree with me, there is nothing on the pages that you and I are looking at that has anything to do with this particular figure as such, is that right?

THE WITNESS: Well --

MR. MARTIN: May I --

THE WITNESS: Your Honor, there are figures in the statements, a part of which figures are represented by the matter that we are discussing.

THE COURT: There is no specific figure that would be directly attributable to the kind of figures that

Mrs. Raimondo had reported to Scansaroli to be in error?

THE WITNESS: That is basically correct, sir, yes.

THE COURT: I understand. Thank you.

Q What is the amount of the provision for deferred taxes, Federal taxes, shown in that financial statement?

A There is an amount for provision for Federal and State deferred taxes of $241,769.

Q What is the difference between the statement that was reported on, which is before you in Government Exhibit 5, and the tax return that was filed?

A I am sorry. What is --

Q The tax return that was filed, was that a consolidated return?

A At that time I don't believe so, sir.

Q Is the report a consolidated report?

A Yes, it is.

Q So are the figures that would appear on the tax return somewhat different thanthe tax figures that appear in the report?

A Yes, they would have been a portion of what appears here. It would be the National Student Marketing Corporation parent portion only, as I recall.

Q As the result of the meetings that you had with Mr. Holloway and Mr.Scansaroli and discussions with Mrs.Raimondo, was the conclusion reached as to the magnitude of the over statement of the deferred tax provision?

A Yes, sir.

Q Approximately what was the amount of that, as best you can recall?

A As best I can recall, it was the entire amount of the taxes thathad been provided on National Student Marketing Corporation's parent portion of the financial statements. My recollection is about $190,000, sir.

MR. MARTIN: Your Honor, do you intend to take a further recess this morning?

THE COURT: I certainly can.

MR. MARTIN: Any way you prefer, Judge.

THE COURT: All right. Perhaps that is a good idea. We will do it right now.

We will take another recess, ten minutes, ladies and gentlemen.

(Recess.)

(In open court; jury present.)

MR. MARTIN: May I proceed, your Honor?

THE COURT: Please do.

Q Mr. Natelli, I put before you Government Exhibit

13, Page 2531.

Would you read the first two entries on that page so that the ladies and gentlemen of the jury know what we are talking about.

A The first of the two?

q That's right.

A The first entry reads, "Debit to accrued costs and unbilled contracts, $489,812. Debit to deferred income taxes payable, $188,750. Credit to unbilled receivables, $678,562 (see explanation for J.E. No. 2)".

Q What is the next entry?

A Entry No. 2, "Debit service revenue, $678,562. Credit cost of service revenue, $489,812. Credit provision for deferred income taxes, $188,750. Explanation,based on subsequent facts, it was decided to adjust three contracts entered into by Ron Michaels, (1) Clairol, (2), Cheseborough, and (3), Ban. This, in effect, is the same as a reclassification entry for report purposes."

Q Did you review that entry at the time it was made?

A I don't recall that I did, no.

Q Did there come a time,sir, that you learned that the entry had been made?

A Yes, sir.

Q How did that come to your attention?

A At some point after the decision to write off the Ron Michaels contracts and the matter of the deferred tax retroactive adjustment being brought to my attention, I asked, I believe, Joe Scansaroli in the course of one meeting what had progressed in terms of those entries having been calculated, the amounts being calculated and the entries being made.

Q What did Mr.Scansaroli say to you on this occasion? Before you tell us that, do you have any recollection of where this conversation took place?

A I believe my office or certainly in the Peat, Marwick's offices in Washington.

Q Approximately when did that occur? Do youhave any recollection?

A I would have to think it was some time in May of 1969.

Q Will you tell us, sir, what Mr.Scansaroli said to you on that occasion as best you can recall?

A The best recollection is that Joe indicated to me that the amounts had been calculated and the entries made and that the amount of the retroactive tax adjustment was very close in amount, very similar in amount to the amount of the Ron Michaels contracts on the books that had to be

written off, that is the gross profit on the Ron Michaels contracts on the books that had to be written off.

I am quite sure, although it is a little hazy -- I am quite sure that he told me that because the amounts were so similar, that he had actually made the entry in the same amount rather than leaving any small net difference between the two.

Q Was there any discussion about any other contract that Ron Michaels had had?

A Yes. I think it was the same discussion, and I don't know if it resulted from my asking a question of Joe or his giving me some further explanation, but somehow or other the point came up that the three contracts that Joe had determined were on the books and to be written off were not all of the Ron Michaels contracts.

To say it differently, my recollection is that he told me that there was an additional Ron Michaels contract that the company either had or was about to write off in the year 8/31/69; in other words, before having brought this matter to their attention as to our decision of how to handle the Ron Michaels contracts.

Q Did you have any discussion about that fact, sir?

A Yes. It was my -- when I heard that I told Joe that unless we knew of anything different as to that one

contract, that notwithstanding the fact that there might be some net resulting difference in amount because this would exceed, therefor, the amount of the tax credit, that the entry should also be made the same way. Presumably the ~~say~~ same reason for that contract being no good is the reason for the other three, so far as we knew at that time.

Q I ask you to turn to the following page, and is there an entry on that page?

A Yes.

Q What is that entry?

A Entry No. 5.

Q What does it state, sir?

A It is "A debit to accrued costs for $49,200, a debit to revenue for $70,200, a credit to cost of sales for $49,200, a credit to unbilled receivables for $70,200. Explanation, to adjust Listerine contract per explanation on J.E.2."

Q Is JE 2 one of the two entries you previously read,sir?

A It is, sir.

Q At the time those entries were made and you had these discussions with Joseph Scansaroli, did you have any intention to deceive or mislead anyone?

A Absolutely not. My intentions were quite the

opposite, sir.

Q Did you intend to do anything other than to make an honest decision on the problem that was presented to you as the engagement partner in charge of the NSMC account?

A That is what I intended to do, sir.

MR.MARTIN: May I have Government Exhibit 14, please?

(Pause.)

Q I put before you, Mr. Natelli, Government Exhibit 14, which is a memorandum from B.J.Kurek to C.W. Randall, date June 3, 1969, in re meeting with Tony Natelli.

Would you, sir, be good enough to read that document to the ladies and gentlemen of the jury.

A Yes, sir. " I met with Tony this morning from 9:30 to 11:00 incidental to our phone conversation yesterday. I reviewed with him the progress our profit-planning and budget were making, the finance committee ideas incidental to a master cash pool and tax effects of consolidated Federal tax returns and stock options. After discussing the above and setting the atmosphere of the meeting, the subject of the meeting was changed to that of NSMC's manner of booking contracts. Cort,quite frankly Tony is very concerned about this situation. Last fall he felt that

the manner in which he allowed us to book contracts would be a cyclical deal. In other words, we would be selling and delivering on contracts in the same quarter that financial reports were made. He now sees the situation as one where commitments either make or break us and we are not performing in the period the sale is made. Furthermore, he anticipates that unbilled receivables could be as high as $4 million at August 31, 1969. If so, he will have to give us a qualified opinion or perhaps no opinion. This is very serious since it could adversely affect our registration this fall. He stated that people working under him are uncomfortable with this situation and if anything were to happen, their certificates and careers would be at stake. Cort, he has reassessed the situation and I feel is rather firm in his conviction and is going to be hard to move. Therefore, due to the seriousness of the matter and my feeling of his conviction, this is a very serious matter for NSMC. I invited him to our finance committee meeting of June 9, 1969, at 3:00 P.M."

Q Do you, sir, have a specific recollection of a meeting with Mr. Kurek as reflected in that memorandum?

A I cannot, sir, say that I recall a specific meeting which this memorandum speaks of.

Q Do you recall, sir, whether in late May or early June of 1969 you had occasion to have discussions with Mr. Kurek in which you expressed concerns about various matters relating to National Student Marketing's accounting?

A Yes, sir. This memorandum may well be of one or perhaps several such meetings.

Q What do you recall about these meetings that you had with Mr. Kurek? Can you separate them in your mind at this time,sir?

A My best recollection is that there was a meeting at which we discussed some concerns that I had and I can't recall all the matters that he portrays here as being part of that discussion.

On the other hand, I am not saying they weren't. I just don't recall them.

Q What is --

A I do recall there was a meeting which was followed by a meeting in New York a short period thereafter.

Q Let's go back first to the meeting with Kurek that you recall. Will you tell us what you recall having

said to Mr. Kurek and what he said to you in the course of that meeting. First, where did that meeting take place as best you can recall?

A I think it took place in our office, but I am not really positive.

Q Do you recall how long the meeting took?

A My best guess would be it was rather short, maybe a half hour or so. But I really can't -- I c-an't be that specific, sir.

Q Do you recall the substance of what was said at that meeting between yourself and Mr. Kurek, what you said to him, what he said to you?

A I recall at that meeting with Bernie that I was expressing to him my very strong concern over the fact that the company had insisted on considering at that point a letter they had received from Pontiac as being an appropriate letter for the recording of the so-called Pontiac commitment. My concern was over the fact that we had agreed at a meeting back in December that on a prospective basis the commitments of the company would be recorded on their books based on a certain form of commitment letter.

Ever since I had been informed about this Pontiac letter I had told Bernie Kurek that it was not the form we had agreed upon and it was different to the extent that

I did not feel it served the purpose that the commitment letter was to serve in terms of representing a firm commitment.

That was the principal matter that I recall being the nature of discussion.

Q I put before you Government Exhibit 12. Is that the letter to which you had reference in this conversation with Mr.Kurek?

A Yes, sir.

Q Would you tell the ladies and gentlemen of the jury what it was in that letter that gave rise to your concerns?

A The letter contains the words "We are now planning to implement student influence proposals that would result in gross billings of 1.2 million dollars," speaking of a total of $1.9 million in the previous paragraph.

The point is, this is now saying, "We are now planning to implement," and we had agreed on some specific language in a commitment letter that would indicate that there was in fact a commitment to use, which was the letter that Mr.Davies and I had drafted.

Q Is that Exhibit G, your Exhibit G, sir?

A Yes.

Q What is the language of that letter to which you

are referring?

A "This is to confirm our verbal commitment to Mr. blank that some time during blank period we will utilize National Student Marketing Corporation to undertake a marketing, promotional and/or advertising program representing a gross billing to us of approximately blank dollars."

Q In addition, was there anything else said at that meeting that you recall having with Mr. Kurek?

A Well, as I am sitting here my recollection is that one of the reasons perhaps for the timing of this meeting is that we had been working on previous to this the so-called first attempt or first draft of a proxy statement and in that connection certain work had been done which was lapsed because of a delay in the eventual proxy filing and it was at a time I think when the company went ahead and issued unaudited six months financial statements. At least, it was around this time, as I recall. It was either something they were about to do or did do.

Hence my reason for extreme concern that they would in their unaudited statements do something, follow some policy that they knew doggone well was something that I did not agree with, and this was also at a period of time when relatively shortly before this we had a question of how to account for income on New England Travel, about which

there was some testimony yesterday from Mr. Holton, and they tried to push me to record income in advance of when I thought it should be recorded on New England Travel.

It was also around this period of time, as I recall, that Mr.Kurek or somebody, either Mr. Kurek or Mr. Randall, but I think it was Mr. Kurek, advised me that they were considering a method of percentage completion accounting on another area of activity, which was for their subsidiary National Manpower Register, which I did not agree with.

What I was concerned about is that the company was becoming aggressive in what they were doing, doing things or trying to do things that I did not agree with.

Here we were in June or thereabouts. I was looking ahead to my next responsibility with this company, which was the 8/31/69 audit, and that is what I was concerned about, and I made sure that Bernie Kurek was aware of my concern, and it is my best recollection that it was I that asked to have a meeting with him and Mr. Randall to make sure that Mr.Randall was aware of my concerns.

I also recall at that meeting, if it is the total meeting or if it was one right within the days around there, that Bernie expressed to me a point of view that why was I getting so concerned about the company's activities

and their unaudited statements and I explained it to him. I didn't want to get into a situation where we would get to 8/31/69, get involved in the audit, and have to do things because the company wasn't following our procedures. He told me -- he understood, I guess -- I can't lay words in his mouth, but he inferred to me that certain officers of the company felt I was being unfair to them because of some of these decisions I was making and I told him if he didn't like it he could sure get some other auditing firm in there.

Q Do you recall anything else about that meeting with Mr.Kurek?

A Not that I recall recall right now, sir.

MR.MARTIN: Mr.Velie, could I please have Government Exhibit 16, I believe it is.

I can use my copy.

Q I show you Government Exhibit 16, Mr.Natelli, which is a document in evidence. Before you testified here today, did you have occasion to review that document?

A Yes, I have.

Q Did you,sir, in fact attend a meeting at National Student Marketing's offices in New York City some time in early June 1969?

A Yes, I did.

Q Do you recall,sir, the date of that meeting?

A I have no reason to contradict this June 9th date that I see here. I am not sure. It certainly wasn't June 10, because that is our anniversary.

Q Certainly it was around that time, is that correct?

A Yes,sir.

Q Where did this meeting take place?

A In the New York offices of NationalStudent Marketing.

Q Who was present as best you can recall?

A My best recollection, without referring to this document --

Q You can use that document if it will refresh your recollection, sir.

A Okay. I can remember Cort Randall being there, Bernie Kurek, I am quite sure I can recall Jim Joy being in and out of that meeting, and I am just not sure of the others, althoughI see their names here. I can't place faces that go with these names at that meeting. They may have been there.

Q At the time you attended this meeting did you know that it was a meeting of the finance committee of

National Student Marketing?

A No, sir.

Q Was there anybody in attendance who was taking notes?

A Yes. In fact, I was surprised that there was because I was not aware it was any kind of a, you know, formal finance committee meeting, but there was --

Q Who was the person who was taking notes?

A Excuse me?

Q Who was the person who was taking notes?

A Someone I recognized as one of the secretaries. I think she may have been Mr. Randall's secretary, though I am not positive.

Q Approximately how long did that meeting take as far as your part in it was concerned?

A Something under an hour.

Q Having reviewed that document, is that a verbatim transcript of what occurred at that meeting?

A No, sir.

Q Does that as best you can now recall reflect at least some of the things that were discussed at that meeting?

A In my reviewing this there are items in it that bring back a recollection of the sense of what took place.

There are some other items that I frankly can't really saythat I recall having happened at that meeting. But essentially overall the sense of the important matters of that meeting as far as I recall them are portrayed in some of those notes,yes.

Q Would you tell us, sir, what you recall occurring at that meeting?

A My recollection of that meeting is that it was a meeting that I attended because I wanted to meet with essentially Cort Randall and Bernie Kurek to make sure that they were aware of my concerns over the fact that they were not at that pointkeeping the agreement we had made as to how they would account for the fixed fee type business on a prospective basis and to make sure that they remembered what I had said about what position we wanted to be in by the 8/31/69 audit with respect to this business, which was that they would have written commitments, that we would be able to make such selection as we wished for written confirmation of those commitments at 8/31/69, and I wanted to make sure that they were thoroughly aware of that in view of the fact that they had for their internal reasons considered the Pontiac document to be adequate, which I did not consider adequate, and that was the emphasis of what took place at that meeting and it was a meeting at which

I may have in fact exaggerated some of the comments I had just to make sure they were aware that I was not about to back off of what I thought the company should be doing.

Q Referring again to Government Exhibit 14, Mr. Natelli, Mr. Kurek wrote in that memorandum, referring to you, "Furthermore he anticipates that unbilled receivables could be as high as $4 million on August 31, 1969."

Did unbilled receivables reach as high as $4 million at August 31, 1969?

A I don't believe so.

Q I direct your attention to Government Exhibit 46C for identification, Footnote 4 appearing at Page 49, and askyou,sir, does that refresh your recollection as to the amount of unbilled receivables reported for the parent company, National Student Marketing Corporation, at its year end August 31, 1969?

A Yes,sir,it does.

Q What is that amount?

A $1,826,962.

Q There is also an amount of Market Research referred to in that. What is that amount,sir?

A $973,226.

Q That $973,226, what did that represent, sir?

A That represented contracts of a subsidiary of National Student Marketing that had been acquired some time late in 1969, W.R.Simmons & Associates, an entirely unrelated matter, but contracts of somewhat similar nature that were being accounted for by that particular firm's independent accountants on a similar basis, as I recall.

Q Who were the independent accountants for W.R. Simmons?

A Unless I stand corrected. I think it was Haskins & Sells.

Q You may stand corrected.

Would it refresh your recollection if I suggested Coopers & Lybrand?

A It was one of the other big eight firms. Coopers & Lybrand it may very well have been.

Q With respect to this question of whether unbilled receivables reached $4 million, did you, sir, cause the company to write off any unbilled receivables of any substantial amount?

A Yes, sir.

Q What was that?

A Well, in the course --

Q Let me put it another way --

A What time period?

Q What happened to this unbilled receivable for Pontiac that had been recorded by the company on the basis of that letter, which is Government Exhibit 12?

A This commitment which the company had booked or this letter which the company felt was a commitment and which they had placed on their books was never accepted by me as a document which should have provided for such recording, and the amount that they had recorded was removed from their books in connection with the preparation of the May 31, 1969 figures for proxy statement.

Q You referred before to National Manpower Registe
Do you recall that, sir?

A Yes, sir.

Q Do you recall, sir, whether or not any entry appears, and I confess I amhaving trouble finding it, in Government Exhibit 13, relating to National Manpower Register? I direct your attention to Pages 2301 particularly -- 2301 to start with. What is that,sir?

A This is a page in the Peat, Marwick work papers on the proxy statement which is a copy of certain post closing journal entries, so-called, as of May 31, 1969.

MR. VELIE: The problem appears to be, your Honor that 2301 is not part of the binder which is Exhibit 13. It may be some other work paper.

MR.MARTIN: There must have been some confusion in putting my papers together. I will offer these pages then

MR. VELIE: Let's see if it is already in evidence.

Q Would you tell us first what page 2301 is, sir?

A 2301 is a copy of a page of post closing journal entries as of May 31, 1969.

Q What is Page 2309?

A It is one of a series of continuing pages of such journal entry,sir.

Q Would you look at Page 2664.

MR. MARTIN: For some reason, your Honor, the confusion is with my copy.

Q Looking at Page 2664 of Government Exhibit 13.

Does that reflect an entry with regard to National Manpower Register?

A Yes, sir.

Q What is the entry that is reflected there, sir?

A Do you wish me to read the entry?

Q No, simply tell us what that entry does, accomplished at the time it was made.

A This entry reverses an entry which the ocmpany had previously made in which they had intended to record income on a percentage completion basis for certain contracts of National Manpower Register to which I referrad previously.

Q What was the amount of the income that was reversed from the company's books?

A Well, the unbilled receivable amount was $207,000 and it appears that the amount of sales and service revenue was $180,144.

Q And the amount of accrued costs?

A $53,460.

Q Would that give you a gross profit of approx-

imately $127,000, is that right?

A Yes,sir.

THE COURT: Are you telling us that you had anything to do with those entries at the time? I don't believe you made those entries.

THE WITNESS: Did I make them, sir? No,sir.

THE COURT: You wouldn't be making entries like that?

THE WITNESS: No, sir.

Q Were those entries made as a result of decisions that you made, sir?

A Yes, sir.

Q What were the decisions that you made that led to the making of those entries?

A The decision I made is that the company should not record income on a percentage completion basis on that particular type of activity in which it was involved.

THE COURT: I see.

Is this as the result of this meeting in June 9, is that it?

A It was something that came to me as a matter that the company wanted to do when they were preparing the May 31, 1969 financial statements, as I recall.

THE COURT: So it was a little later than June?

A The eventual entry, sir?

THE COURT: No. You tell us that you apparently got the company to reverse this entry or entries, right?

THE WITNESS: Yes, sir.

THE COURT: What I am trying to find out is, when did this occur? On the negative side, perhaps, I am trying tofind out whether it was discussed at this June 9th meeting,which I thought you just told us about, in New York City.

THE WITNESS: I am not sure if that particular item was discussed at the June 9th meeting. It was about that period of time that the matter was first brought to me for consideration by the company, by Mr. Kurek, as I recall. Then there was a -- there were a series of meetings between that time and the time the eventual entry that we just spoke of was written in, which the company continued to try to persuade me that what they wanted to do was correct or was an appropriate method of accounting, I should say.

I continued to give consideration, as I always would, to any arguments that they would raise, but it was my final decision, and that entry results -- reflects the results of my decision, sir, that that method of accountin

is not appropriate in this particular instance.

THE COURT: It was some time between, let us say, June and the end of August?

THE WITNESS: Yes, sir.

Q I place before you Government Exhibit 13 and I ask you, sir, to look at that document for a minute. First tell us, Mr. Natelli, the original proposal for National Student Marketing to prepare a proxy, what were the unaudited figures that were to appear in that, if you recall?

A It was originally to be the unaudited figures for the six months ended February 28, 1969.

Q Did there come a time, sir, when a decision was made that the proxy would not be printed with figures for February 28, 1969, but would be printed with figures for the following quarter, May 31, 1969?

A Yes, sir.

Q Who advised you of that and what were you told in that regard, as best you can now recall?

A As best I can recall, it was a telephone call from either Jim Joy or perhaps Mike Matthews of White & Case, both of whom would normally have been discussing matters of acquisitions with me and, in fact, matters pertaining to the proxy perhaps with me. I am sorry, did I not answer the question?

Q What did they tell you at this time?

A I was advised that the proxy that had been commenced was to be postponed or was being postponed and figures at a later date were to be used -- I am not sure it was to be determined at that point what figures, at what later date, because there was a matter which had come up unexpectedly that would require a proxy solicitation to the shareholders, as I understand it, and that the company felt or the advisors to the company felt that it would be a waste of effort to go to the shareholders with two proxies in a relatively short period of time.

The matter which had come up, as I understand it, was the prospective merger of the Interstate National Corporation with National Student Marketing Corporation.

Q Directing your attention to the first few pages of Government Exhibit 13, those marked 2515, 16, 17, 18 those pages, sir.

Would you tell the ladies and gentlemen of the jury what those pages repreesent?

A These pages represent notes made by me in the course of the overall preparation of the proxy statement or, more specifically, the financial statements that were to be included in the proxy statement. That is the financial statements as of May 31, 1969. They were my notes as to

things that I at this particular point in time realized required some attention, concern or action, either. It is a series of notes of various types.

Q Were these notes made at the time that the February proxy was being prepared or were they notes relating to the May proxy?

A It appears to me that they refer to the May proxy in these particular pages.

Q What is it in those pages that indicates to you it relates to the May proxy?

A There are comments relating, for example, to Interstate National Corporation which, for one, would not have been a matter that would have been the subject of a proxy that was being contemplated with the February 1969 figures.

Q How many review notes did you make there, sir?

A Thirty-two.

Q Of those 32 review notes that you made in connection with the preparation of the May proxy, how many of those notes relate to unbilled receivables?

A I believe there is one note pertaining to unbilled receivables.

Q Just to give the ladies and gentlemen of the jury some idea of the other problems that were there,

would you look, for example -- let's pick Note 15, and tell the ladies and gentlemen of the jury what that note provides, states, and the type of problem that you had under consideration at the time you prepared it?

A Note 15 happens to be "Where do we stand as to new opinion on E.P.S.?" -- which means earnings by share -- "re" -- regarding "shares to be issued in future on acquisitions."

Note 2, which presumably must refer to some note in the contemplated draft of the financial statement, but I am not sure -- it has to do with an accounting consideration that I felt had to be taken into account in the process of preparing these financial statements.

Q What is the note that you made relating to unbilled receivables? What note number is that and what does that state?

A It is Note No. 10. It is headed under a series of notes pertaining to NSMC. There are various groups of notes here, some of which pertain to some of the acquisition companies that were coming in to NSM at the time.

It says,"Review all unbilled contracts and all deferred costs to determine reasonableness."

Q Is there any entry made in connection to that note?

A There is an entry that indicates "Done," with the initials D.H.O.

Q Who is D.H.O.?

A It should be Doug Oberlander, sir.

Q I want to place before you, Mr. Natelli, Government Exhibit 17B, which, as you know, has been identified here and the ladies and gentlemen of the jury all know are three pages. These are, as has been testified to here, Mr. Natelli, a footnote on the financial statement or some of the footnotes to the financial statements as they appeared in the original draft of the proxy statement, a similar page from the original draft on which there are some handwritten notations.

Whose handwritten notations are those?

A They are mine, sir.

Q Then this is a portion of the final proxy as it was printed going to the original draft, Notes C, D and E, who originally drafted those notes?

A I am quite sure that I did.

Q Particularly withregard to the Note D, which contains a number of figures for the years 1966, 1967 and 1968, do you recall --

A I believe it is Note E, sir.

Q I am sorry. Note E.

A Yes.

Q Do you recall who actually collected the data and inserted the figures in the footnote that was drafted.

A No, I do not know who would have actually put the figures in the columns.

Q Did you put the figures in the columns as best you can recall?

A I don't believe that I did.

Q What was the practice at Peat, Marwick, Mitchell & Company with regard to notes drafted by partners that needed some figures inserted in the notes?

A I would say it was quite usual for the partner to draft the so-called narrative portions of the notes and delegate to individuals working under him the function of filling in the figures that would pertain to the notes.

THE COURT: Mr. Martin, in view of the hour, if you are going to go into another phase of this, I wonder if you would mind if we stopped. There are some matters I want to take up with counsel before luncheon.

MR. MARTIN: Your Honor's pleasure is my pleasure.

THE COURT: All right.

Ladies and gentlemen of the jury, we will suspend now so far as you are concerned and we will resume Monday morning at 10:00 o'clock.

I believe from what I hear that there is a fair chance we might finish the testimony and evidence on Monday.

Am I wrong in that, gentlemen? I said only a fair chance.

MR. MARTIN: I would say that there is a fair chance. I thought your Honor had some other commitments on Monday. I misinterpreted --

THE COURT: No. I worked on rearranging those since I spoke to you early this morning and my problems are not going to be a block on Monday.

With that in mind, is that a fair statement for the jury, before we say goodbye to them for the weekend?

MR. MARTIN: I think a fair estimate, subject to our problems on all estimates.

THE COURT: I am not trying to pin you down. Certainly you are not the only one involved.

But I think that is the best we can say. That will give you some idea, in any event, ladies and gentlemen.

I hope you have a pleasant weekend. See you at ten o'clock Monday morning.

Could you come into the robing room briefly, gentlemen, with the reporter.

(Jury left the courtroom.)

(In the robing room.)

(Discussion off the record.)

THE COURT: I am concerned about time sufficiently to say that I would hope -- I have received your requests to charge and I am ready to rule upon them any time I get a chance -- I would hope that we could start summing up on Tuesday at some point.

Would you agree to that, that that looks likely?

MR.VELIE: Yes, your Honor.

MR. MARTIN: I would certainly hope so, your Honor. I think I will be another half hour to 45 minutes, the best estimate I can give you.

THE COURT: You are going to be at least that with this gentleman, and I am afraid Mr. Velie is going to be a long time, no matter what he does. But I am hopeful we can go along.

I have canceled my long standing commitment to go to Danbury Prison because I think it is well worth it that I do so. Much as I regret having to do it, it is

more important that we keep going here.

How much time, roughly, do you want to sum up? You can think about that over the weekend and tell me on Monday.

MR. MARTIN: I will think about it. I have also handed in and I don't know if the clerk has yet given you a memorandum in which I suggest that some consideration be given to the order of summations.

THE COURT: That is thought to be a great problem by a great many wise men or allegedly wise men in our profession. I regard it as an absolute tempest in a teapot. But I am willing to think about it. Coming from responsible types like you and Mr.Stillman, that is what I will do.

MR. MARTIN: Thank you, your Honor.

THE COURT: I will have to tell you as a general proposition I think it is meaningless. But great and wise people across the country say otherwise and who am I to question their judgment. However, it is not yet the law.

MR.MARTIN: I recognize that, your Honor. I do think it would have one salutary effect in shortening summations.

THE COURT: I don't believe it, but I said

I would certainly be glad to think about it.

MR. STILLMAN: Judge Tyler, the program then is to push ahead, assuming we finish testimony on Monday, summations Tuesday, or if we finish testimony Tuesday, commence summations on Tuesday.

THE COURT: No. We are not going to take chunks of time out if I can help it, unless there is some really good reason. But I don't want to do that.

There is not, contrary to other myths in our profession, any prejudice in that. I sat around watching that too long to fall for that old chestnut.

You see, the jury has every reason to look to get now to come to an end. I don't mean to say that you should cut anything out, but I think our duty is plain.

Have a good weekend.

xxx (Court Exhibit 4 marked for identification.

(Adjourned to Monday, November 11, 1974, at 10:00 A.M.)

United States of America

vs. 74 Cr. 43

Anthony M. Natelli and
Joseph Scansaroli

New York, New York.
November 11, 1974 - 10:00 A.M.

(Trial resumed.)

(In open court; jury present.)

A N T H O N Y M. N A T E L L I resumed.

MR. MARTIN: May I proceed, your Honor?

THE COURT: Yes, sir.

DIRECT EXAMINATION (continued)

BY MR. MARTIN:

Q Mr. Natelli, you may recall when we concluded on Friday we were discussing the original draft of the proxy statement.

MR. MARTIN: Your Honor, I want to offer one page of an additional binder. Can we mark this as Natelli Exhibit U-1 for identification.

xxx

(Defendant Natelli Exhibit U-1 was marked for identification.)

MR. MARTIN: Would you mark that as Natelli Exhibit U for identification.)

xxx (Defendant Natelli Exhibit U was marked for identification.)

Q Mr. Natelli, I show you Natelli Exhibit U-1 for identification. Would you tell the ladies and gentlemen what that binder is?

A It is a binder from the files of Peat, Marwick, Mitchell containing some miscellaneous data regarding the 5-31-69 proxy of National Student Marketing Corporation.

Q I have marked as Natelli Exhibit U a copy -- is that a copy of a page from that document?

A Yes, it is.

Q Would you look at the original, sir, and tell us whose handwriting appears at the top of that page as best you can recall.

A It is my handwriting at the top of the page.

Q Would you identify the last of the items on that page that you can identify as being in your handwriting

A Read it, do you mean?

Q Yes.

A The number 3 and then the words "B. Kurek -Wash." for Washington, the abbreviation for Washington.

MR.MARTIN: Your Honor, I would offer Natelli Exhibit U for identification through the entry that Mr. Natelli has identified as being the last one in his hand-

writing into evidence. May the record reflect that I am showing both to Mr.Velie.

MR. VELIE: May I ask just a question or two?

MR. MARTIN: Sure.

VOIR DIRE EXAMINATION

BY MR. VELIE:

Q Mr.Natelli, you didn't date this page, did you?

A The page is not dated where it says date. There is a date indicated on it, however.

Q Whose writing is this where it says JS, and then something off on the side?

A It is my writing.

Q This writing on the side underneath where it says JS, did you write that at the same time that you wrote this other material which you have identified?

A I would say that I wrote it either at the same time or later than I wrote the other material.

Q So that your testimony is that these entries reflect something earlier, you say, than August 4, is that correct?

A Yes, sir.

MR. VELIE: I have no objection.

xxx (Defendant Natelli Exhibit U was received in evidence.)

BY MR. MARTIN:

Q Mr. Natelli, will you now tell the ladies and gentlemen of the jury what Natelli Exhibit U is.

A This is a copy of a work paper on which I listed information for White & Case, the attorneys who were handling the proxy for National Student Marketing Corporation, identification of parties that we knew or we felt should receive copies of the proofs of the document that was being prepared, that is, the proxy.

Q Would you read the note that Mr.Velie was referring to which appears on the side of that paper?

A Yes. There are initials JS, which would mean Joe Scansaroli, my addressing this paper to him, if you will, and the words "I gave this information to Matthews this morning 8/4/69," with my initial, A.N.

Q Who is indicated on that document to receive copies of the proofs of the proxy statement, and I would ask you to confine yourself to those entries which are in your hand.

A The entries that are in my hand read in three [redacted]groupings, the first grouping PMM, meaning Peat, Marwick, Mitchell, designation of copies, four copies to C.Breslin, PMM Chicago, one to L. Otkiss, PMM Philadelphia, three A.M.Natelli, PMM Washington.

Then there is an item for Interstate, Number 5 for five copies to D. Jeffers at Interstate. Then for NSMC, one copy J. Joy New York, and three B. Kurek, Washington, or Wah for Washington.

Q You indicated a Mr.Breslin at PMM Chicago. What was Mr.Breslin's relationship to this proxy?

A Mr.Breslin was the Peat, Marwick, Mitchell partner in our Chicago office who had the client responsibility for Interstate National Corporation, which happens to be a client of Peat, Marwick, Mitchell & Company prior to any association with National Student Marketing Corporation.

Q You tell us that that document indicates that five copies of the proof of the proxy were to go to Mr. Jeffers. Who was he?

A Mr. Jeffers was I believe the comptroller -- I am not positive of the title, but I believe the comptroller at Interstate National Corporation.

Q You will recall, Mr. Natelli, that when we concluded on Friday we were discussing the footnote that appears in the draft on the right-hand side of this footnote page. I believe you told us that you did not insert the figures in these columns, is that correct?

A Yes, sir.

Q When you drafted the footnote that now appears here -- the number, just for identification, is 3750005 on that page -- what figure did you intend to appear here on the line "Retroactive adjustment for contract losses"?

THE COURT: Do you understand that question, Mr. Natelli?

THE WITNESS: Yes, sir.

THE COURT: All right.

Q What number did you intend to have appear on that line?

A The amount that would reflect the caption, that is, the total amount of the revenue of the contracts that were being written off retroactively to 1968. I don't recall the number without referring to something, sir.

Q Do you know the approximate number?

A $700,000 approximately.

Q Do you recall being asked in the grand jury if you could explain how it could have happened that instead of the $700,000 figure a figure of $70,000 was inserted in there by the person who inserted the numbers? Do you recall being asked that in the grand jury?

A Yes, I do.

Q Can you explain that?

A I believe I can explain how it might happen, yes, sir.

Q Would you do that, please.

A The information --

MR. VELIE: Excuse me. I am going to object to that question as calling for speculation.

THE COURT: That is what I am a little concerned about here. That is why I raised the question I did a moment ago. I am frank to say, Mr. Martin, the record reflects as of Friday afternoon and again this morning that he didn't supply the figures.

MR. MARTIN: All right.

THE COURT: Therefore, for that simple reason I am a little unsure as to just what this means.

Second of all, it may possibly mean, among other things, as Mr. Velie now is suggesting by his objection, that we are just speculating, which I don't think is particularly helpful.

MR. MARTIN: All right. Let me try it another way, your Honor.

Q Where in the proxy binder that is before you would an accountant who was attempting to get the information necessary for this footnote go to get the figures?

MR. VELIE: I object again. I think the "who" suggests to us that he is asking Mr. Natelli to speculate on a matter he may or may not know. If he knows I have no objection to his being asked about it.

MR. MARTIN: He is an accountant, your Honor, and would know where to look, obviously.

THE COURT: Of course. But that doesn't get to the fundamental problem here.

As I understand it, Mr. Natelli, you say that you had nothing to do with those figures which appear on the draft proxy page which Mr. Martin has delineated for us by number, correct?

THE WITNESS: Yes. I don't recall that I inserted those figures, that's right, sir.

THE COURT: Did you have anything to do at the time with checking any work papers to see whether or not the figures were correct?

THE WITNESS: No, not that I recall, sir.

THE COURT: Then I don't understand how we can proceed on this basis, Mr. Martin.

Q I direct your attention to page 2530 of that

binder, sir. Tell us what that is?

A Page 2530 is a trial balance of the accounts representing the information which would go into a statement of earnings for National Student Marketing Corporation, portraying information pertaining to the company as it existed at May 31, 1969, reflecting its position, however, as it would have been at August 31, 1968, with inclusion or as a result of inclusion of the companies that were pooled thereafter.

Q What is the first column on that page?

A The first column --

MR. VELIE: Objection. I want you to lay a basis, if you can, by asking Mr. Natelli if he either prepared that page or worked with it at the time the proxy was done.

MR. MARTIN: Your Honor, this page has already been identified in evidence as a trial balance.

THE COURT: Fine. That is one reason I am puzzled by this. If it is already in evidence then you can make any arguments that seem right.

You have had the witness tell us two things. One, he did not prepare the figures. Two, he did not check them. I see no point in belaboring him or the time of all of us if you can bring it out anyhow, being in evidence, as it

apparently is. At least, according to my notes it is.

MR. MARTIN: Fine, your Honor.

Q Mr. Natelli, you notice that the second or middle panel of this exhibit reflects some changes made and I believe you identified these as being in your handwriting, is that correct?

A Yes.

Q Would you tell the members of the jury the circumstances leading up to your making those changes which appear on that exhibit?

A Well, in the process of reviewing the first draft designated by the page we were just previously discussing, to the left on that display, what I would be doing is looking at what had already been drafted and seeing if it was appropriate in the circumstances and so on, and in the case of this particular item I would have been reviewing what had been drafted by me as the appropriate notes in the circumstances, based on my first draft.

MR. VELIE: Excuse me. I believe that answer is unresponsive in that it speculates as to what he would have been doing and he was asked what in fact he did do.

THE COURT: Perhaps, but it may be a semantical problem. Some of us talk in that way.

When you say you would have been do you mean that

you did or are you just guessing?

THE WITNESS: No, I am just giving a past tense. Perhaps my English is not proper.

THE COURT: You mean you did?

THE WITNESS: I did, yes. Sorry for the flaw in the English.

THE COURT: It's all right. Go right ahead.

A I was reviewing the draft as I had originally prepared it and in the process was considering whether the information there was what I would go forward with, and so on, and in the case of this particular note what happened was that I looked at the note that explained narratively at that point what the retroactive adjustments were in the 1968 statement of earnings and in reviewing the words that I had used my feeling was at the time that they didn't really give an appropriate explanation of what I was trying to put forth and the more I thought about it the more I felt that I would have to get more into an explanation of the specifics of the so-called Ron Michaels matter, the unethical conduct of an employee ~~a pro~~.

I believe that I also made some attempts on separate pieces of paper, which I don't now have, at trying to expand that note in order to say more about this particular situation, the Ron Michaels write offs.

In the process of doing that I found it very difficult to come out with words that would do what I was trying to do and, frankly, I started becoming concerned about putting into a public document such as this information about an individual's conduct, and the more I looked at it and the more I realized, as indicated in the first narrative portion of that note, that the net amount of the total adjustments at that point that we were talking about was only $21,000, the more I began to feel that this was trying to explain something that in the final analysis was not very meaningful.

In addition, the other factors that I had in mind as I was going through this process, was that the company had changed very significantly from August 31, 1968, as it had originally been reported, up to the time that we were now looking at the company, as of May 31, 1969.

It was a larger company. The figures were certainly not as material.

And the other factor is that we were now looking at a situation where the fixed fee contracts, which were the items we were dealing with here, were items that were based on written commitments as opposed to the situation which existed when we first went into the company, where they were oral commitments.

And my conclusion after looking at all that information and considering all that information was that it really seemed meaningless to make the narrative disclosure about this item.

Q Before making the final decision as to the changes which are reflected on that page, did you discuss this matter with anyone?

A Yes, I did.

Q Who did you discuss it with as best you can recall?

A I'm quite sure that I discussed my feelings about the matter with Joe Scansaroli at the time. In addition, I spoke to Mr. Otkiss in Philadelphia, who was the SEC reviewing partner, and --

Q Would you tell us what the conversation you had with Mr. Otkiss was, as best you can recall?

MR. VELIE: Excuse me one second.

(Pause.)

A In essence, the conversation with Mr. Otkiss was pretty much what I just described to you.

Q Can you fix a time of this conversation?

A It would havebeen sometime between the initial draft of the proxy and the subsequent draft of the proxy after inclusion of the changes that are indicated in the middle there.

It is sometime in August. Beyond that I can't give you a specific date.

Q Would you tell us, as best you can recall, what the conversation was that you had with Mr. Otkiss on this

subject?

A I described to Mr. Otkiss my consideration in reviewing the draft of the note that I had originally set forth, just as I have described them here. I don't know if you want me to repeat all that. It was essentially what I just described here.

And my conclusion or tentative conclusion, that it really was meaningless to go through a lengthy explanation which was difficult at best when the net effect of what we were dealing with was a $21,000 adjustment to the net earnings of the company in 1968.

Q Did Mr. Otkiss state whether or not he agreed with your conclusion?

A Yes, he did state that he did agree with my conclusion.

Q You said one of the factors that led you to conclude that disclosure of this particular item was not necessary was that the company had changed substantially between August 31, 1968 and the time that you were working on the proxy, is that correct?

A I believe those are my words, yes.

xx (Defendant Natelli's Exhibit V marked for identification.)

Q I show you, Mr. Natelli, what is now marked as

your Exhibit V.

Could you tell us what that is?

A Yes. It is a copy of a memorandum that I wrote on June 16, 1966 to Mr. Breslin in our Chicago office.

Q He is the man you have identified as being the Peat, Marwick partner who was responsible for Interstate as a client of his, is that correct?

A Yes, sir.

MR. MARTIN: Your Honor, I would offer that document in evidence.

MR. VELIE: No objection.

xx (Defendant Natelli's Exhibit V for identification received in evidence.)

MR. MARTIN: May I read the exhibit to the jury, your Honor?

THE COURT: Surely.

(Mr. Martin read from Defendant Natelli's Exhibit V in evidence to the jury.)

Q Mr. Natelli, directing your attention to the final panel on this exhibit, that reflects the same footnote that we have been talking about, footnotes, as they appeared in the final version of the proxy, and you have heard testimony, sir, that in this footnote the items that you have crossed out, the full amount of the Ron Michaels contract

ended up being subtracted from the pooled companies line.

You are familiar with that testimony, aren't you, sir?

A Yes, sir.

Q Were you aware of that fact, Mr. Natelli, at the time the final proxy was being prepared?

A Well, I don't recall focusing on that aspect of it heavily.

On the other hand, I certain reviewed the drafts of the proxy and was aware of what we ended up with in that note.

As a result of recently going over these documents in the course of trial preparation, I would say that there is -- there are certainly indications on the document that I must havebeen aware that this is what happened, that the amounts were adjusted in the net pool line.

Trying my best to recall the situation, it would have been quite logical or it was quite logical that this is where the adjustment ended up. This is a note that has as a primary objective the showing of a trend of net earnings of NSM as between the form that it was when it was originally reported in its previous report with whatever companies were involved and as it now existed with whatever companies were involved. Since we had concluded at that

point that it was not necessary to make any narrative disclosure, logically the amount would fall into the line, ifyou will, that represented an adjustment from the previously reported to the presently reported company as it now stood.

That must have been the logical conclusion as to where it ended up.

Looking at it now, I probably should have inserted the words on that line which reads pooled companies or whatever the full caption is. I can't see it from here. I probably should have included the words and adjustments on that line, but that obviously not was done.

Q At the time you prepared this proxy, did you intend to mislead or deceive anyone?

A No, sir.

Q Were you attempting to cover up anything?

A No, sir.

Q Did you intend to defraud anyone?

A No, sir.

Q Did you believe at the time that proxy statement was prepared that it was false and misleading, sir?

A No, sir.

Q When did you first hear of any large commitment from Eastern Airlines, as best you can recall?

A I have a vague recollection that I heard about it

sometime in August of 1969. I believe that I may have heard about it from Cort Randall during conversations in which I was expressing to him my conclusion that the Pontiac agreement or Pontiac letter was not adequate for recording on the companies books, and I believe at some point he may have mentioned that there was an Eastern contract which they expected to be receiving within days at that time.

Q Where did this conversation take place, as best you can recall it?

A I have a vague recollection it was mentioned to me by Mr. Randall during some telephone conversations in August.

Q Can you fix this conversation with relation to the time that you went to the printers in August?

A It would have been right prior to that occasion.

Q I show you what is now your Exhibit H.

MR. MARTIN: May I read this to the jury just to set the context to the questions?

THE COURT: All right.

(Mr. Martin read from Defendant Natelli Exhibit H in evidence to the jury.)

Q Mr. Natelli, do you recall the conversation to which Mr. Kurek refers in that memorandum?

A No, I can't say that I recall this specific conver-

sation.

Q Did you have occasion to discuss with Mr. Kurek in the course of the preparation of the proxy the Pontiac commitment?

A Yes, I'm sure that I asked Mr. Kurek whether they had received on the Pontiac letter anything more definitive, that is anything in the form of the commitment letter, in the commitment letter format that was to be used for commitments.

Q Do you recall what his response was?

A I am sure that he told me that they did not yet have it, but I can't recall any specific conversation, sir. I just know it was a topic that was of concern at the time, and I am sure I would have asked Mr. Kurek about it once or more than once.

MR. MARTIN: Could I have Exhibits 18 and 21?

(Pause.)

Q Did there come a time, Mr. Natelli, that you went to the printer with certain people from National Student Marketing and Mr.Scansaroli?

A Yes, sir.

Q When did that occur, sir?

A The middle of August, the end of August 14, 1969.

Q Can you tell the ladies and gentlemen of the jury the circumstances that led to you going to the printer on that occasion?

A We had been working or my staff had been working on the draft of the proxy during that particular time frame with a view toward just getting it into the printer as soon as was possible. There were some target dates, and I don't recall what they were, but I think we were kind of running up against target dates all the time, taget dates that had been set basically by the attorneys, White & Case,

who were primarily responsible for the proxy.

I believe it may have been that on that particular day was one of those target dates that we were supposed to go to New York to -- not go to New York necessarily, but have some amended proofs to New York for the printer which was not accomplished.

We didn't -- during the course of the day we hadn't gotten to a point that that was able to be done.

Some time during that afternoon, as I recall, or early evening we were asked that in spite of the fact that we didn't have it done yet, we were asked to go to the printer to complete the work right there at the printer so that the information could be put in print, if you will, over the course of that night and the next day.

Q While you were at the printers that night and the following morning, were there figures that had been prepared for the May 31, 1969 period?

A I believe that by the time that we had left for the printers we had the consolidating trial balances complete with certain figures as of May 31, 1969, that is the company did work in conjunction with our people.

Q Do you recall whether there was any discussion at the printers as to the Pontiac commitment?

A Yes, there was additional discussion, if you will, about the Pontiac commitment.

Q Tell us what you can recall about that discussion. Who was present and what was said and the time that it occurred, if you can fix that?

A I find it difficult to place any particular time frame except that it must have been early upon our arrival at the printer that I indicated to probably Cort Randall andBernie Kurek that I didn't really understand why we had to push to get these figures in print when we knew at this point that they would have to be changed again or something to that effect.

It was probably some time that evening.

MR. VELIE: Excuse me. I thought Mr. Martin asked him who was present.

Q Who was present, do you recall?

A In addition -- I believe the conversation was with Mr.Randall and Mr. Kurek. I think it was probably in the presence of whoever was there in this big room that we were working in on the proxy. I am really not positive. It was certainly wherever we were working.

Q Was it a nice quiet room like this courtroom, Mr. Natelli?

A No, there were people working around a couple of

tables in the room. There was a group of attorneys working in one section of the room on the so-called fore part of the proxy, Joe Scansaroli, I believe John Stalick, Bernie Kurek and perhaps John Buck, I guess, and I were working at another very large table at another end of the room, and there was a lot of conversation going on by people about what they were doing, some proofreading, so on.

Q Did everybody stay in their one seat all night?

A No, of course not. There was moving back and forth within the room and in and out of the room.

Q All right.

You are telling us about a conversation where you raised the question about the numbers not being final, in any event.

Did you indicate why you believed the numbers were not final?

A Yes, because at that point the Pontiac figures were in the May 31, 1969 numbers, and there had not been at that point a more definitive document on which that commitment could be booked.

Q What was Mr. Randall or Mr. Kurek's response to that statement, as best you can recall?

A Well, as best I can recall, it was within the context of that discussion that I was advised that the

company did expect to have or did have -- I can't remember which at this point -- a letter from Eastern Airlines, a commitment letter from Eastern Airlines, which they wanted me to consider to be includable in those May 1969 figures since they apparently -- I guess it was during that evening that they kind of gave up on the fact that they would be able toget the -- the time had run out, so to speak, in trying to get a letter from Pontiac.

Q You say there was discussion about an Eastern commitment and it being includable perhaps in the proxy statement.

Was there any discussion as to what changes would have to result from the Eastern contract being includable if it was accepted?

A My recollection is that what the company wanted to do was to simply substitute the documentation for the Eastern contract in place of what was the documentation for the Pontiac contract without making any adjustments in the financal statements as of May 31, 1969, as they were then prepared.

I believe that their feeling was that the amounts were of a nature that just -- if you will, a substitution of documentation could be made. That is what

they were asking me to consider.

That is what they were recommending.

Q How would that affect the figures that appeared in the proxy?

A There would have been no change in the figures that were in the proxy.

THE COURT: You keep saying "they." Who are "they"?

THE WITNESS: I would say it was Mr.Randall -- the conversation as I recall was Mr. Randall, Mr. Kurek and I, although there may have been others present.

But it would have been Mr.Randall making this recommendation to me, sir.

2nd 2B

THE COURT: In other words, it was Randall?

THE WITNESS: Yes, sir.

Q I show you a document marked Government Exhibit 21D for identification, and ask you to tell the members of the jury what that is.

A 21D is once again a binder of work papers from the Peat, Marwick, Mitchell files. In this case it is a so-called asset binder having to do with the 8/31, that is, August 31, 1969 audit.

MR. VELIE: Just a point of clarification. That is Exhibit 21. What you see as a D is ID, which stands for identification.

THE WITNESS: I see.

Q Directing your attention to part of that binder, Page 3120, which is Government Exhibit 21 in evidence, would you tell the members of the jury what that is.

A That is a document, a rough set of notations, if you will, in my handwriting, which contains certain considerations or indications of certain considerations that I had been making in connection with the discussion of the Eastern contract, Pontiac contract, at the timeof the proxy -- at the time of the printers, at the printers.

Q Can you tell from looking at that document, sir, what was the subject being discussed at the time that

memorandum was prepared?

A I believe that the subject being discussed was the question that had been raised by the company to me, the recommendation of simply switching the Eastern contract for the Pontiac letter.

Q What would the effect of that adjustment be on the figures in the proxy?

A I believe the consideration at this point was to simply switch the documentation without any changes in the figures in the statement of earnings.

Q What is the last notation that you wrote on that document other than any figures that might appear on there? Would you read that to the jury?

A It is an Item 5, "All figures in proxy would have to change. I estimate a good 30 to 40 hours work. Cost $600 to $1000 for accounting alone."

Q Does that item help refresh your recollection as to the subject that was under consideration?

MR. VELIE: I object to that. I don't think that there is any refreshing needed here.

THE COURT: Sustained.

A Well, the point --

Q The objection is sustained.

THE COURT: No.

THE WITNESS: I am sorry.

Q If you decided simply to insist on removing the Pontiac contract without accepting the Eastern contract would the proxy have had to be reprinted?

A No, obviously not. That was the company's recommendation, that we just leave the figures as they were and accept one set of documentation in place of the other.

Q Ultimately, sir, what did you decide on that question?

A I decided that that was not an acceptable solution to this matter.

Q Ultimately, sir, did the company record in the proxy statement the income from the Eastern Airlines contract?

A Yes, sir.

Q Did the proxy have to be reprinted to accomplish that?

A Yes, sir.

Q I show you Government Exhibit 18 and ask you, sir, to tell the members of the jury what that is.

A Government Exhibit 18 is a copy of a letter dated August 14, 1969, from Thomas Mullen of Eastern

Airlines to Robert Bushnell, National Student Marketing Corporation, confirming a verbal commitment of May 14, 1969 to use NSMC services.

Q When did you first see that document as best you can recall?

A On the afternoon of August 15.

Q Where did you see it?

A At the printer's location.

Q Would you tell us the circumstances that led to your receiving that document?

A My recollection is that some time that day, in the morning, I was told that the company had in fact obtained the letter that they had been expecting would be forthcoming on the Eastern Airlines commitment, that it would be brought over to the printer's offices.

Q You say Mr. Kelly brought that, is that correct?

A No, I didn't say that. I said it would be brought over to --

Q WAs it brought over to the offices?

A Yes, it was.

Q By whom?

A My recollection is that Mr. Kelly brought it over.

Q Did he have anything else with him at the time he brought that letter?

A Yes, he did. He had a copy of the underlying program or proposal that was the subject of this commitment letter.

Q I show you, sir, what is Government Exhibit 24 for identification and ask you to tell us what that is.

A Government Exhibit 24 is once again or yet another binder of Peat, Marwick working papers prepared in connection with the National Student Marketing Corporation proxy statement. This one has a heading on it "Pro forma statements 1969."

Q I direct your attention to the last group of papers in that and ask you, sir, beginning at Page 2240, if you can identify that. That is also the original, a copy of which is now your Exhibit J in evidence. Would you tell the members of the jury what that is?

A This is a series of papers dealing with the Eastern contract. The top page is a summary of information, which is in my handwriting, which lists figures and dates of time from time records of Mr. Bushnell, who was the account executive for the Eastern Airlines program.

Q Would you look, sir, at Page 2267 and the unnumbered page that should be I think 2268 and tell us

what that part of the document is and when you received it.

A This part of the document is a copy of the proposal which is headed "Eastern Airlines Youth Marketing Plan 1970," which has a notation on the cover "Submitted May 9, 1969," and it is the -- a copy of the document that Mr. Kelly brought to the printer's office on the afternoon of August 15.

Q Will you tell the ladies and gentlemen of the jury what occurred when Mr. Kelly came to the printer's office with these documents?

A Yes. The purpose of Mr. Kelly coming to the printer's office was for me to meet with him so that I could discuss this Eastern commitment contract with him and obtain from him an explanation of what the various elements of the program were so that I could gain some appreciation of what was involved in the program and make a determination as to whether or not it was the type of business that was being accounted for as fixed fee type business.

Q There are some notations that appear throughout that presentation, particularly, if you look, for example, at Page 2275. Whose notations are they?

A They are my notations, sir.

Q When were they made?

A They were made at that time, when I was meeting with Mr. Kelly and getting from him information such as I thought appropriate.

Q Was a decision reached on Friday August 15, 1969 as to whether or not you would have any objection to the company including this Eastern commitment in the proxy figures?

A No, sir.

THE COURT: I don't follow that. When you say "no, sir," you say there was no decision made on that day?

THE WITNESS: Yes, sir, that's right, that's what I say.

THE COURT: All right.

Q When, if you can recall, was such a decision made?

A Sometime the following week, probably the early part of the following week.

Q Directing your attention to the first pages of Natelli Exhibit J, page 2240 through 2265, of the proxy binder in front of you, tell the members of the jury when you received the documents that start at 2242 and what you did when you received them.

A I can't tell you exactly when I received those documents. I can tell you that they were received in Washington some time after the visit to the printers, which probably would have meant the following Monday, since I don't believe that I was in my office over that weekend.

The information within the pages that you have

indicated represent time logs from the files of National Student Marketing Corporation for Mr. Bushnell and the top summary, which I indicated before is in my handwriting, represents summation of information from those time logs for time spent by Mr. Bushnell on the Eastern program.

xx (Defendant Natelli Exhibit W marked for identification.)

Q I show you, sir, your exhibit W for identification and ask you would you tell us what that document is, without relating it to the specific items that it reflects?

A This document is what we call a telephone charge posting ticket from the files of our Washington office.

Q Is that type of document one that is made in the regular course of the business of Peat, Marwick Mitchell and Company?

A Yes, it is, sir.

Q Is it a regular course of business to make and keep such records?

A Yes, sir.

Q Is the entry that is reflected thereon made at or about the time of the transaction which it reflects?

A Yes, sir.

MR. MARTIN: Your Honor, at this time I would offer Natelli W for identification in evidence.

MR. VELIE: No objection.

xx (Defendant Natelli Exhibit W received in evidence.)

Q Would you tell us, sir, what Defendant Natelli Exhibit W is specifically?

A This is a telephone charge slip which indicates that I made a telephone call to Mr. Dennis Kelly at a New York number, area code 212 PL. 8-7700, on August 18, 1969.

Q Do you recall what that telephone number was?

A I am quire sure it was National Student Marketing's offices, sir.

Q Do you recall the substance of that conversation with Mr. Kelly?

A I cannot say that I have a recollection of the specifics of the conversation at that time.

Q Ultimately, did you come to a conclusion whether or not it would be acceptable for the company to record in its unaudited statements for May 31, 1969 a commitment from Eastern Airlines?

A Yes.

Q What was that conclusion, sir?

A It was my conclusion that they could include this item.

Q At the time that that conclusion was reached, did you believe that it was appropriate for the company to record that commitment?

A Yes, sir.

Q Were you trying to defraud anybody when you came to that conclusion, sir?

A No, sir.

Q Were you attempting to mislead or deceive anyone?

A No, sir.

Q Did there come a time, Mr. Natelli, when Joseph Scansaroli left Peat, Marwick, Mitchell and Company?

A Yes, sir.

Q When, as best you can recall, did that occur?

A October '69, probably the beginning of October, somewhere in that period.

Q At any time prior to the time he left Peat, Marwick, Mitchell and Company, did Mr. Scansaroli tell you that he was concerned that he might lose his certificate because of the 1968 audit of National Student Marketing Corporation or any other event that had occurred?

A No, sir.

Q Did you ever hear anyone at Peat, Marwick, Mitchell make a statement about losing their certificate?

A Never in any serious vein. From time to time it

is not uncommon for members of the staff in a joking vein, after they have dealt with some particular difficult matter, to jokingly say "Hope we don't lose our certificates over this one."

That kind of thing, yes, sir.

Q Is there anyone that you have known personally that has ever lost their certificate as a CPA?

A No, sir.

Q Did you ever hear Mr. Scansaroli say anything about losing his certificate?

MR. VELIE: Objection. That has been asked and answered and he doesn't like the answer.

MR. MARTIN: That has not been asked and answered.

THE COURT: I understood the witness to say that he never heard Scansaroli say that he feared that he might lose his certificate.

Am I correct about that, Mr. Natelli?

THE WITNESS: That he feared -- that's correct, sir. I don't recall Joe saying that he feared losing his certificate.

THE COURT: So you are making some distinction?

MR. MARTIN: Yes, your Honor.

THE COURT: What is the distinction, so it is not lost on anybody else?

MR. MARTIN: Your Honor, I asked the witness did he ever hear Mr. Scansaroli say he was concerned about losing his certificate.

THE COURT: This is a distinction.

MR. MARTIN: That's right.

THE COURT: If you feel it is I won't sustain the objection.

You see his point, Mr. Natelli?

THE WITNESS: Yes, I do.

A Yes, I believe, although it is a hazy recollection, I believe that Joe may have also in a joking vein at some time or another said, "Hope we don't lose our certificates over this one."

It is the kind of thing that Joe might say, the same way he said at one point as we chatted about, "I don't get paid to make those kind of decisions," a wise-crack remark.

THE COURT: In other words, the distinction you and your lawyer are trying to make here is the only time you might have heard him say anything like this was in jest?

THE WITNESS: Yes, sir.

THE COURT: All right.

Q Are you able to fix a time, do you have any

recollection as to when this incident might have occurred?

A It may have been at the time the Ron Michaels contract writeoff problem came up.

I can't be sure about that.

Q I show you another one of these work paper binders which has been marked Natelli 1 for identification --

THE COURT: Excuse me. That can't be so.

Q I'm sorry, ~~National Student Marketing 1~~ Natelli L for identification.

Can you tell us what that is?

A It is a folder of miscellaneous work papers from the Peat, Marwick files, once again pertaining to National Student Marketing Corporation.

Q Page 8671 of that, can you tell us what that is?

A Yes. It is a handwritten notation or note from me to bill, in this case that would mean Bill Colona.

Q Is that the same note that has been copied and now appears on Natelli Exhibit N?

A Yes, sir.

MR. MARTIN: May I just show the original of this to the jury, your Honor?

THE COURT: All right.

MR. MARTIN: Ladies and gentlemen, that is the original of the note which appears on the cover of the other document we have Xeroxed and used and introduced in evidence.

Q Wouldyou read to the ladies and gentlemen of the jury what you wrote on that document? Tell us, when was

that prepared?

A I can't give you a date from this document, but it would have been at such time as I decided that Bill Colona would replace Joe Scansaroli as the supervisor on the National Student Marketing engagement.

Consequently, it would probably be in October of 1969.

Q What did you state in that note to Mr. Colona at that time?

A It says, "Bill, attached is program for contracts at National Student Marketing Corporation. Please get into this as first order of business. Satisfy yourself that procedures are adequate," with my initials.

Q Did you have any discussion with Mr. Colona about that?

A I can't recall any specific discussion at the time of handing him this, but I'm sure that in the process of giving Mr. Colona background on his assignment, I would have discussed with him the facts behind this document, that is, my asking John Johnston to work on it and my completing it and so on.

Q Did there come a time, sir, when Peat, Marwick, Mitchell had to prepare a comfort letter in connection with the Interstate merger that was the subject of the proxy?

A Yes, sir.

Q Do you recall having any discussions with anyone at Peat, Marwick, Mitchell concerning that subject?

A I'm sure that in the course of the month of October I advised Bill Colona to be sure that he took into account as one of the items that were now his responsibility the fact that we would have to issue such a comfort letter next with the Interstate closing.

Q Do you recall whether or not you had any conversation with Mr. John Johnston on this subject?

A Yes. Sometime in the beginning of the last week of October, I believe it was on a Monday, I chatted with Johnny Johnston to make sure that this comfort letter was something that was on the program to be accomplished within that week, and asked him if he had given consideration to this or make sure that he was giving consideration to this.

Q Did he say anything to you at that time about the matter?

A My recollection is that at that time that he hadn't really gathered all the information necessary, but we were in the process, of course, of doing the 8-31-69 audit. Johnny was the assigned senior, and I believe he mentioned to me some of the adjustments that he knew were proposed adjustments for the 8-31-69 audit that were of some signifi-

cance and might have a bearing on the wording of the comfort letter.

Q Do you recall what he mentioned in this regard?

A I'm really not sure. I think he at that time probably mentioned the deferred charges as a particular area, that is the deferred charges for the PI programs. I think he had some analysis of that and had some indication of that being a problem.

There may have been also the item on the additional paid in capital adjustments. I'm not sure if we had any other information beyond that at that time.

Q Do you recall what you responded to Mr. Johnston in this regard?

A Well, I told him to make sure that in the course of the next couple of days he got into this to make a final determination of what the adjustments were that would have an impact on the comfort letter, and I also called to his attention the fact that we would have to take into account whether any of these adjustments reflected back on the May 31, 1969 figures which was one of the elements of the comfort letter that was required.

Q Directing your attention, sir, to Thursday, October 30, 1969.

Did you have occasion to speak to Mr. Colona on

that day about the comfort letter?

A Yes, sir.

Q Was that conversation in person or by phone?

A By phone.

Q Where were you at the time, sir?

A I was at home. I had just returned from a visit to the doctor's office. I had taken some X-rays.

Q Approximately what time of day did this conversation occur?

A It was late afternoon some time.

Q Do you recall what the conversation was, what Mr. Colona said to you and what you said to him?

A Mr. Colona was reporting to me on the results of the work that he and Johnny had been doing on the comfort letter during that week, and he ad--Mr. Colona had advised me of in summary what problems they had identified, and in substance I believe he had some tentative draft of some wording that would have to go into the comfort letter ~~was~~ regarding the matters that had been identified.

Q Was there any discussion of the magnitude of these adjustments?

A Yes, I believe at that point he had identified the $300,000 of the receivables, the $500,000 of the deferred charges and whatever the amount was for additional paid in capital adjustments.

Q What, if anything, did you say to Mr. Colona?

A I told Mr. Colona that -- first, I believe I asked Mr. Colona if the company was aware of our findings, and he told me that they were, that he had been, of course, working with Mr. Kurek in the process of doing this work.

I then told him that because of the seriousness of the adjustments that we had, I felt that this was a significant problem in the comfort letter and told him to -- first thing in the morning, since it was late in the afternoon -- the first thing in the morning to call Mr. Otkiss as soon as he got in the office, who was the reviewing partner in Philadelphia, and discuss the matter with him since I wasn't sure whether because of the illness that I had, whether I would be able to get into the office the next day.

In essence, I said look, whether I am there or not, you go ahead and call Mr. Otkiss first thing in the morning.

Q Did you go to the office the following morning?

A Yes, I did.

Q Did you have occasion to speak to Mr. Otkiss?

A Yes, I did.

Q Would you tell us what you said to Mr. Otkiss on that occasion and what he said to you?

A Mr. Otkiss had already been called by Mr. Colona. So he already had knowledge of the basic problem we were dealing with.

I got in the office a little later than Bill did. We, in essence, reviewed with one another the problems that had been identified and Mr. Otkiss felt every bit as concerned about this as I did; in fact, to the extent that he suggested that rather -- because of the seriousness of the matter, that we should telephone Professional Practice Department, Mr. Holton in particular, and discuss the matter with him.

Q Did you have occasion to have such a conference call with Mr. Holton?

A Yes.

Q Prior to that did you have any contact with anyone at National Student Marketing Corporation?

A My recollection is that I spoke to Bernie Kurek, probably a combination of in my office and by telephone. He was in the vicinity of our office. His office was in the vicinity of ours. I believe he was there that morning with the intention of picking up the comfort letter and bringing it to New York.

I believe that I also -- before wespoke to Mr.

Holton, I believe I had also contacted Mr. -- they are Mr. Joy and Mr.Davies or one or the other of those two individuals in National Student Marketing's New York office or White & Case' office, somebody in New York from National Student Marketing.

Q Do you recall the substance of any of the conversations you referred to with Mr. Kurek, Mr. Joy or Mr. Davies?

A Well, basically -- Number 1, with Mr. Kurek, I asked him what the status of things were as the result of the comfort letter and he indicated that, you know, he was -- I think he may have used the words he was just a messenger by that morning, there to pick up the letter and bring it to New York, that it was in the hands of the people in NSM in New York, so I should contact them. In essence he understood that the closing was going to be going ahead so far as he knew.

Q What about your conversation with Mr. Joy and Mr. Davies? Do you recall anything about those?

A I have a very hazy recollection of calling them, but I do have a recollection that during that morning it was my understanding that the company was planning to go ahead, that the Interstate people had -- who were going

to be participating in the closing were aware of the fact that there would be the comments that were in the comfort letter, but that the company was -- they were planning to go ahead with the closing, as I understood it.

Q Would you tell us, sir, what occurred in your conference call with Mr. Holton and Mr. Otkiss?

A We brought Mr. Holton up to date as to what had transpired and -- that is the contents of the draft, comfort letter at that point, what we had planned to put in it, advised him that there was a closing imminent that day, that it was taking place at the White & Case offices and, in short, by the time that conversation was ended, it was left that I would get a draft as it then stood of the comfort letter communicated to White & Case and our New York office for Mr. Holton.

Mr. Holton was going to consider as the result of our conversation, consider the matter that we had discussed himself and I presume with others in New York.

Q Did you communicate the contents of the comfort letter to the people at the closing at White & Case?

A I didn't do it personally, but we did communicate a draft to the people at White & Case, yes.

Q Subsequently during the day were additional portions or additional paragraphs added to the draft that

had been communicated to the people at the closing?

A Yes, sir.

Q I will refresh your recollection, sir. I put before you Natelli Exhibit K in evidence, which contains the final comfort letter.

Would you tell us what additions were communicated to the parties at the closing as best you can recall?

A Some time that day I recall having communicated to the people in New York at White & Case. I believe I communicated to John Davies, but I am not positive about that, the fourth from last paragraph which starts out, "Your attention is called, however, to the fact that if the four adjustments had been made," so on.

Q Did you have any conversation about that with the people that you were talking to at White & Case, with Davies or anybody else?

A Yes. I believe it may have been after I communicated that paragraph to the White & Case offices that there was a phone call between me and Mr. Davies and Mr.Epley, who was also on the phone at that time, wherein in short the companies -- that is, there was an objection raised by both of these individuals to this paragraph being included in the letter, their feeling being that it was gratuitous and unnecessary since all it did was summarize information that was in previous paragraphs.

Q Was there any further discussion that you can recall with Mr.Davies or Mr. Epley on that day?

A Well, I think in that particular phone call what happened was I told them that whatever their feelings on that paragraph, this is something that we had considered, that I felt was absolutely necessary be put inthe letter, that it had been a matter of discussion already with our executive office, who was -- which was involved in the letter by this time, and we felt that this was a necessary paragraph.

I believe it was also in that discussion that I told him that at this point I wasn't sure what else would go

into the letter as it was then drafted before we arrived at a final conclusion of the letter. I advised him that it was under consideration in our executive office, that the letter, because of the timing problem at that point, the letter would be issued by our executive office, that it could be mechanically completed during that day, and I think it was also in that conversation that I said to Mr. Epley that in addition to any wording in the letter we had under consideration what other steps the company perhaps should take.

In fact, I think it was in that particular conversation that I said that we were considering the fact that the company perhaps should go to -- should bring this matter to the attention of the SEC. I think it was in that same phone call.

Q Did there come a time that you learned that the closing had taken place?

A Yes, sir.

Q Looking at the first page of Natelli Exhibit K, did you have any discussions with Mr. Holton about his sending a letter to each member of the board of directors of National Student Marketing Corporation and Interstate National Corporation prior to the time that letter was sent?

A Yes, sir.

Q In any of the conversations you had with anyone on the day the comfort letter was issued or with the people who worked on your staff in the preparation of that comfort letter, did you suggest to anyone that you would have a personal problem if this merger didn't go through or the fact of these adjustments came to the attention of the SEC?

A Absolutely not.

Q Did you at that time have any concern about your own personal situation, that you had done anything wrong?

A No, sir.

Q I show you what is now your Exhibit L in evidence. Again, for background, would you tell the members of the jury what that is.

A This is a letter dated November 20, 1969, addressed to me from JohnDavies, general counsel of National Student Marketing Corporation.

Q Would you read the substance of that letter, the body of that letter, to the members of the jury?

A "Bernie Kurek has requested that I advised you whether or not the principals of Stuckey & Speer, the Cottrell Bus Company and the Ritzenthaler Bus Company were advised of the October 30, 1969 comfort letter delivered by Peat, Marwick to us in connection with the Interstate Nationa transaction. They were so advised and in fact delivered

to us a letter acknowledging that they had been so advised.

Q Would you tell us about the circumstances that led up to your receiving that letter.

A Yes, sir. As a result of the problems that had arisen in connection with the issuance of the comfort letter I advised Bernie Kurek that he should be sure as the financial officer of NSMC that companies that were then in negotiation for acquisition by NSMC, which companies had received information by way of the proxy about NSM, should be informed that the proxy information was in fact in error to the extent of the matters that we had noted in our comfort letter to the company.

Q Had this idea been suggested to you by anyone at the Peat, Marwick New York or Philadelphia offices?

A No, sir. I don't believe that anyone in either of those offices was aware of these transactions that were taking place at that time, as we were in Washington.

Q When you told Mr. Kurek that these companies should be given the comfort letter and told of the adjustment to the May 31, 1969, figures were you trying to cover up the adjustments that had been made in the May 31, 1969 figures, sir?

A No, sir.

Q Mr. Natelli, you are a defendant in a civil

action brought by the SEC, is that correct, related to this matter?

A Yes, sir.

Q Prior to the time that that action was instituted had you ever been the subject of any type of disciplinary action or any action by the Securities and Exchange Commission?

A No, sir.

Q Have you ever been the subject of any criminal proceeding before, sir?

A No,sir.

Q Did you, sir, in preparing this proxy do what you considered to be an honest job at the time?

A Yes, sir.

Q Did you ever intentionally participate in the preparation of this proxy knowing that it was false or fraudulent?

A No.

MR. MARTIN: I have no further questions.

THE COURT: Ladies and gentlemen, we will take the morning recess at this point.

(Recess.)

MR. STILLMAN: I have no questions, your Honor.

MR. VELIE: May I proceed?

CROSS-EXAMINATION

BY MR. VELIE:

Q Mr. Natelli, September of 1968 -- you have the time fixed in your mind -- that is the very outset, is it not, or pretty much the outset of your engagement with National Student Marketing, is that correct?

A Yes, sir.

Q At the very outset of your engagement in 1968, September, did you do some checking to see why the price of National Student Marketing stock was as extraordinarily high as it was?

A I can't recall doing any particular checking, no, sir.

End 5A

Q Do you recall having some discussions with Jim Joy a number of times concerning the high multiple of the company's shares, the shares were then trading in the 70 to $80 range? Do you recall that?

A I remember having discussions with Jim Joy about the multiple of NSM stock, yes, sir.

Q You and Mr. Joy were determined to find out if there was any hanky panky driving the price of that stock up as high as it was, isn't that correct, sir?

MR. STILLMAN: Your Honor, I must object to this. I don't see what that has to do with this lawsuit.

THE COURT: Overruled.

A I can't recall anything in that context, no.

Q Is this your signature, sir? I am showing you Government's Exhibit 59 for identification.

A Yes, sir.

Q This is, is it not, a memorandum you sent to your partner, Mr. Phillips, on September 19, 1968?

A Yes, sir.

Q Take a look at the clipped paragraph here at the bottom of the second page. Read it to yourself.

Have you read enough to see if you used the word hanky panky, sir?

A I read enough to see that that wasn't my word,

yes, sir.

Q You didn't put the word hanky panky in your memorandum which you sent to Mr. Phillips?

A Yes, that's in that memorandum.

Q Mr. Joy advised you then that he was constantly checking to see if there seems to be any hanky panky going on behind the scenes, is that correct?

A That's what that seems to say, yes, sir.

Q Do you recall assuring Mr. Phillips, your partner, "Naturally, we will, of course, keep our eyes and ears open and continuously evaluate any information which comes into our hands in workingwith thisclient."

A Yes, sir.

Q You did that right at the very outset, is that correct?

A Yes, sir.

Q You kept your eyes and ears open.

I believe you told us you were the partner in charge of the 1968 audit, is that correct?

A Yes, sir.

Q You told us you were responsible for that audit? Is that your word?

A Correct.

Q You signed the opinion in Government's Exhibit 5,

which is the annual report for 1968, is that correct?

A Correct.

Q Incidentally, Mr. Martin asked and you said that that opinion is addressed to the board and the shareholders of National Student Marketing. That's correct, isn't it?

A Yes.

Q You didn't mean to suggest by that that you weren't responsible to the public for the material that went in there, did you?

A No. I was answering Mr. Martin's question.

Q I see.

Well, did you think it important to tell this jury that the responsibility of a public accountant is not only to the client who pays his fee, but also to investors, creditors and others who may rely on the financial statements which he certifies?

A It is certainly appropriate.

Q That certainly is an important piece of information, isn't it?

A Sure.

Q The annual report for 1968 is a public document, is it not?

A Yes, it is.

Q It became part -- do I have this right -- it became

part of a 10K report filed with the Commission?

A Yes, sir.

Q Available for members of the public to look at to see what National Student Marketing was all about?

A Correct.

Q You were responsible then not just to the Board and to the shareholders but to members of the public?

A I was responsible to do what I thought should be done as a certified public accountant.

Q You knew that National Student Marketing was actively seeking to acquire other companies for its stock. didn't you?

A Yes.

Q In fact, one of the very first things you learned about the company when you went to get a feel for the company, I think your word was, was they were in the middle of pitching some company to acquire it, is that correct?

A Maybe if you tell me what you mean by pitching I can answer the question, sir.

Q They were telling what they were all about, talking about their business and so on, trying to induce another company to be acquired, isthat correct?

A Yes, they were explaining their activities to another company.

Q They wanted to make a good impression on that other company so that they could acquire it, isn't that correct?

A I presume that's a two-way street in those situations, yes, sir.

Q Of course, you knew that the price of this stock was very high, isn't that correct?

A I would have had some knowledge of the price of the company's stock, yes, sir.

Q I asked you if you knew it was high.

A In relation to what, sir?

Q In relation to its earnings.

A High in relation to its earnings in terms of having a certain multiple, yes, sir.

Q It had a very high multiple, didn't it?

A Once again, a high multiple, I don't know what you would be comparing it to. But yes, a high multiple.

Q It was not secret to you that if they showed a loss in the 1968 report the price of the stock might tumble?

A That is something that might happen, yes, sir.

Q Wereyou aware of it?

A Was I aware of the tumbling?

Q Were you aware that the price of the stock might

tumble if they showed a loss?

A Sure, I was aware that in the normal course of events thatmight or might not happen.

Q In fact, Mr. Scansaroli wrote it down in the work papers, didn't he?

A I am not sure whether he wrote down exactly what you are trying to portray here, sir.

Q Did Mr. Scansaroli write down in Government's Exhibit 3 at page 1913 "If we don't record them," meaning the contracts we have all been talking about here, "We will probably show a consolidated loss for the year and many stockholders would sell their stock," is that correct?

A That's correct, but I don't think it relates to the previous question. But I can stand corrected.

Q Selling their stock, doesn't that have an effect on the price?

MR. MARTIN: I object.

A It could have, but I don't know --

MR. MARTIN: It is argumentative.

THE COURT: I will allow it.

Q It could.

A It could have, but I don't see how you could get that conclusion from reading that document. He was obviously talking about the reported earnings of National Student

Marketing Corporation and he doesn't mention anything about marketing price in that document.

Q Tell me, sir, you knew that in mid-October for the very first time the company came up with these $1.7 million in sales, is that correct?

A I knew that when I first heard about these fixed fee contracts, whatever they ended up being in amount, they had not yet been recorded on the books, if that's what you are saying, yes, sir.

Q You first heard about them in October, is that correct?

A As I say, it is either the end of September or the beginning of October, yes, sir.

Q The documents which Mr. Scansaroli gathered together in his special sales work papers largely dated October 17 and 18 as back up for these contracts, is that correct?

A That's right.

Q Those records represented the very first records with respect to these contracts, is that correct?

A Obviously after information had been gathered, yes, sir.

Q All right.

It was no secret to you that the year had ended two months before, is that correct?

A Correct.

Q Did you ever check with people at Arthur Andersen to see, in fact, how the company had been handling these contracts throughout the year?

A I didn't personally, no.

Q Mr. Scansaroli told us he didn't either.

Did you think somebody else had?

A I'm quite sure that I asked Joe Scansaroli how

these contracts would have been accounted or had been accounted for during the previous year, at which time Arthur Andersen were auditors.

Q Let me see if I have it right.

You asked him to check with Arthur Andersen?

A I believe I asked Mr. Scansaroli how Arthur Andersen had dealt with these contracts. That's not quite what I said in the previous answer, that's the substance of it.

Q Did Mr. Scansaroli come back and tell you that he hadn't checked with Arthur Andersen?

A My recollection is that Mr. Scansaroli advised me that the extent of any of this type business in the previous year was ~~negligent~~ negligible, practically non-existence, and this, in fact, is one of the reasons why we were discussing this problem at this time. It was a new area of activity that the company had gotten into during the year.

Q I thought I asked you if you had asked Mr. Scansaroli to check with Arthur Andersen and Mr. Scansaroli reported back to you that he didn't? Did he advise you of that, sir?

MR. MARTIN: Objection, your Honor. There are two questions there. Let him ask one at a time.

MR. VELIE: He's answered the first one.

MR. MARTIN: I object, your Honor. He has not

answered the first one.

THE COURT: Let the jury decide that.

Now that we have gone this far, why don't you put the question again in one simple question form.

Q Did Mr. Scansaroli ever tell you that he never checked with Arthur Andersen?

MR. MARTIN: I object to that as argumentative.

THE COURT: Overruled.

A I don't recall Mr. Scansaroli telling me that he didn't check with Arthur Andersen.

Q Did you havean impression that he must have checked with Arthur Andersen?

A I had an impression that he knew from the contact that he had had with Arthur Andersen and the review of the work papers that Arthur Andersen that he had performed, that he knew what the status was of this type business as of the preceding year, yes, sir.

Q That was the impression you had?

A Yes, sir.

Q Did you have the impression that Mr. Scansaroli might have read the management letter prepared by Arthur Andersen?

A I don't recall having any particular impression regarding the management letter at all.

Q You didn't read it yourself, did you?

A No, I didn't.

Q If you had you would have known that they were counting on written contracts, wouldn't you?

MR. MARTIN: Objection, he's asked about a document he didn't read.

THE COURT: I will sustain the objection. However, if you want to develop a theme with this letter, you may.

MR. VELIE: Yes, your Honor.

Q Government's Exhibit 68 for identification, that is the management letter, isn't it, prepared by Arthur Andersen in July of 1968, one month before you began your engagement?

MR. MARTIN: Objection.

THE COURT: Just a moment. There is an objection?

MR. MARTIN: Yes, sir.

THE COURT: Yes, I will sustain that form at least because of something he suggested or said a moment ago.

Q You told us you didn't check the Arthur Andersen letter at the time.

No question in your mind but Government's Exhibit 68 is the Arthur Andersen letter, is it?

MR. MARTIN: Objection.

THE COURT: Have you ever seen this before, Mr.

Natelli?

A Have I ever?

THE COURT: That document in front of you.

THE WITNESS: Yes, I believe I have seen it previous to today, sir.

THE COURT: Next question.

Q In your review of it did you happen to know that they contemplated written contracts?

MR. MARTIN: Objection, your Honor.

THE COURT: Is there an objection?

MR. MARTIN: Objection.

THE COURT: That objection will be overruled.

MR. MARTIN: I think we should fix the time when the witness saw the document.

THE COURT: We will in good course I assume by one or the other.

MR. VELIE: Please read the question to the witness.

(Question read.)

A I would have to re-read it at this time to answer that question.

THE COURT: Perhaps you can help him, Mr. Velie.

MR. VELIE: Yes, your Honor.

Q Why don't you read here on page 15 where it says,

"Desirable procedures should provide."

MR. MARTIN: Objection, reading from a document not in evidence, your Honor.

THE COURT: We don't have to read it. I'm not accepting your basis. I agree with you for other reasons. We don't have to read it. Just point what you want him to read.

Q Read the sentence here, Mr. Natelli.

A Does that mean I should only read this sentence?

THE COURT: To yourself. If you want to read anything else, you may.

A Thank you, sir.

Okay, sir? What was the question.

Q They did contemplate signed contracts, didn't they?

MR. MARTIN: I object to that, your Honor.

The witness cannot testify to what Arthur Andersen did.

THE COURT: I agree. Sustained as to form.

Q In your review of this document, Mr. Natelli, when you reviewed it did youfind that in July Arthur Andersen was recommending the use of signed contracts?

MR. MARTIN: Objection, your Honor. The document hasn't even been authenticated by anyone at Arthur Andersen. This witness didn't prepare it and didn't see it until after events --

THE COURT: The latter may be true, but I still think there is a fair question.

MR. MARTIN: I press the authentication objection, your Honor.

THE COURT: The witness states that he has reviewed the matter. That is sufficient for our purposes on cross-examination in my judgment.

Put the question again because of this colloquy between counsel and the Judge so the witness understands you, sir.

Q In your review of this document, do you find that Arthur Andersen, in fact, contemplated the use of signed contracts in July of 1968?

THE WITNESS: Your Honor, I have a problem in answering that question with respect to July 1968, which I would be glad to explain to you, sir.

THE COURT: In other words, you can't answer the

question?

THE WITNESS: Because I have seen other documentation which leads me to wonder about the date on this document.

Q Let's ask it without the date, Mr. Natelli.

In your review did you find that Arthur Andersen contemplated the use of signed contracts?

THE COURT: Or at least this letter so indicated.

A This letter indicates that they are recommending to the company that the company on a prospective basis account for or get into administration of this business on signed contracts, yes, sir.

Q You didn't take the trouble to read this then, did you?

A I never saw it, sir.

MR. MARTIN: Objection,your Honor.

THE COURT: Gentlemen, just a moment. Aside from the point made by counsel, I think it is objectionable on another ground.

What do you mean by that?

Q Did you take the trouble read this when you were supervising the audit in 1968, Mr. Natelli?

MR. MARTIN: Objection, asked and answered, your Honor.

THE COURT: I believe that is what you stated, that you never had occasion to read this or some copy thereof until long after the event, isn't that so?

THE WITNESS: That is quite a different question from what I was just asked, yes.

THE COURT: That is the reason for my intervention, Mr. Natelli.

You did not read it, say, in the summer or the early fall of '68?

THE WITNESS: That is correct.

THE COURT: Could you tell us, so we won't have any more arguments on this point, about when it was that you had occasion to read it, a copy of this letter?

THE WITNESS: The first time I saw that document was whenit was provided to me to look at by the Securities and Exchange Commission in the course of my testimony before them. As I understand it, it represented a document that they had acquired as a result of their subpoena powers.

THE COURT: That would be in 1970 some time?

THE WITNESS: '71, I believe, sir.

THE COURT: '71?

THE WITNESS: Yes, sir.

THE COURT: Thank you. Go ahead.

Q Mr. Natelli, it is no secret to you that accounting firms prepare management letters, isn't that correct, as part of their usual practice?

A That is correct.

Q Your firm prepares them?

A Yes, sir.

Q They talk about internal control procedures, do they not?

A Do the letters talk about internal control procedures?

Q Yes, sir.

A My wording would be a little bit different than yours, but in substance that is correct.

Q Internal control procedures in substance are those which are of some concern to an auditor, are they not?

A Yes,of some concern.

Q If they are weak the auditor must extend his procedures to make sure that his audit is reliable?

A Correct.

Q All right. Did you take the trouble to talk to Mr. Sullivan, whom the evidence has indicated was an accountant who might have something to do with contracts in progress accounting in the May 1968 period?

A No, I did not.

Q You heard Mr.Scansaroli I believe say that he did not either, is that correct?

A He may have testified to that effect, yes, sir.

Q Did you ask Mr.Scansaroli to check with Mr. Sullivan?

A No, I did not.

Q Your counsel, Mr. Martin, offered -- I believe this is in evidence -- Natelli Exhibit C, these pages from Mr.Sullivan's work papers.

A Yes, sir.

Q Did you take the trouble to review these pages while you were supervising the audit, sir?

A Once again, I can't answer that question in the way you have asked it because I did not see or know of these particular work papers at that time.

Q Let me just ask you: Do I understand it that you didn't talk to Mr. Sullivan?

A Yes, sir.

Q Do I understand it that you didn't ask Mr. Scansaroli to talk to Mr. Sullivan?

A That's correct.

Q Did anybody give you to understand that he had checked with Mr.Sullivan and found out what the deal was with respect to Sullivan's work?

A Did anybody, meaning whom?

Q Anybody. Did anybody tell you among your -- let's take the people who are doing your audit. Anybody assure you that the step had been taken of checking with Mr. Sullivan just to see how, in fact, these contracts had been handled only several months before?

A Well, if you would permit me to give you a complete answer rather than a yes or no, it might be explanatory.

Do you want me to answer it yes or no, or give you an explanation?

Q I thought I asked you did anybody ever tell you that he checked with Sullivan?

A Yes, Mr. Kurek had worked with Mr.Sullivan.

Q Mr. Kurek told you he had checked with Sullivan?

A Mr. Kurek told me that he had worked with Mr. Sullivan in preparing those figures.

Q What steps, if any, did you do to check either work papers or have work papers checked to see thatyou rea-ly had the true story with respect to the May figures?

A In the sense of what I considered necessary at the time, no steps were taken.

Q This exhibit is in evidence and I am going to read the last paragraph of it. This is Mr. Sullivan's hand -

writing.

MR. MARTIN: Wait a minute.

(Pause.)

MR. VELIE: Mr. Martin tells me they might have come in as B, just so the record reflects that. I am reading what I believe to be C. It came in as B.

Q "The company's procedures appear reasonable where there is a definite commitment by the client as represented by a signed contract, memorandum or other documentation and an actual expenditure of time and costs to the program."

Just so there is no confusion about it, you didn't check that piece of paper when you supervised your review, is that correct?

A That's correct.

d 6B

Q You were aware, were you not, Mr. Natelli, that all of these sales which came up in mid-October were the difference between a profit and loss for National Student Marketing, isn't that correct?

A I believe I have indicated earlier I am not sure that I was aware that it was a difference between a profit and a loss, but I certainly was aware that it was significant to the company's results, yes, sir.

Q You did direct Mr.Scansaroli to make a case for the contracts, is that correct, in your own writing?

A I am sorry. If you would like to give me what I said perhaps I can answer that yes or no.

Q Page 1470 of Government Exhibit 4C for identification. This is your handwriting, isn't it?

Let me just see if I have the right place, Mr. Natelli.

First of all is that your handwriting?

A Yes, it is.

Q Have you seen the point at which I have pointed on Page 1470?

A Yes, I certainly have.

Q You said, didn't you,"In other words, establish a case from the facts as to why we should have the contracts booked as of August 31, 1968."

A That is part of what I said, sir.

Q You said that?

A That is part of what I said, yes.

Q Did you say that?

A Yes, I said that plus what goes before it, sir.

Q There is about 50 pages to this exhibit.

A But that is one sentence of one particular note, sir. I would be glad to read the whole note for you if you wish.

Q Why don't you.

A "Prepare an analysis of the income for FY 67 and 68 showing type programs which yielded the income, that is, straight poster jobs, direct mail programs, etc., question why haven't the contracts in process been a problem previously. In other words, establish a case from the facts as to why we should have the contracts booked as of August 31, 1968."

Q No question in your mind but that Government Exhibit 3 is the case that Mr.Scansaroli established, isn't that correct?

A Those are the work papers pertaining to this area of work, yes,sir.

Q That was responsive to the very note you read us, was it not?

A I believe so.

Q Did you take the trouble to read it while you were supervising this audit?

A No, I did not read in detail.

Q Did you read the introduction to it? It is three pages long.

A I believe I may have, yes.

Q You simply forgot about the sentence then that says "If we don't record them we would probably show a consolidated loss."?

A I may have forgotten it up until this time, but I hear you read it now.

Q So that you did know that it was the difference between a profit and a loss, isn't that right, Mr. Natelli?

A As he indicates, it was probably a difference between a profit and a loss. He used the word "probably" probably because he wasn't sure at the time either. I don't know.

Q In fact, it was the difference between a profit and a loss, wasn't it?

A As we have seen, yes, sir.

Q You have heard Mr.SCansaroli testify that without adequate records contracts in progress percentage of completion accounting was chancey and inefficient. You

don't dispute that, do you?

A I don't dispute he made that statement, no, sir.

Q Do you dispute the truth of what he said? It is chancey and ineffective, inefficient, to try to account for contracts in progress on a percentage of completion basis when you have inadequate records, that's true, isn't it?

A Well, in view of the way that question came up it was probably a fair answer to the question. I would say that basically it is true that percentage of completion accounting requires adequate recordkeeping, yes, sir.

No question about that, is there?

A No, sir.

Q Did you take the trouble to read Mr.Scansaroli's conclusions on Page 1970 of Government Exhibit 3 that the company had, in effect,no records with respect to these contracts?

A Once again, I probably was aware of what he said at that time. I believe I may have read that summary.

Certainly that was the problem that we knowingly faced in the consideration of this problem at that time. So that is not something that is being brought to my attention for the first time by any means, or the attention of anyone. It has been inthose documents since 1968.

Q You were certainly aware of the fact that the salesmen were not even entitled to their commissions yet on these so-called sales, weren't you?

A I am not sure what my knowledge was of the commissions at that time. I believe I raised the question of Mr. Scansaroli as to whether or not the commissions were payable to them, to the account executives, if that is who you are referring to, at that time, yes, sir.

Q The question was of sufficient concern for you to write a note for Mr. Scansaroli to check, is that correct, to find out in effect whether they can get their commissions on these sales at this point?

A Yes, I believe that is correct.

Q Mr.Scansaroli answered that for you, didn't he?

A I can't recall what the answer is.

Q He told you probably not, didn't he, at Page 1470 of Exhibit 4C?

A It says "Probably not, he does receive advances."

Q You know that an advance against a commission is a kind of a loan, don't you?

A It is a kind of a loan?

Q A salesman is not entitled to it until he earns the commission, isn't that correct?

A That would be a fair statement, yes.

Q You were responsible, weren't you, for the proper supervision of that audit?

A Yes.

Q In carrying out your responsibility did you okay the practice of oral confirmation?

A Yes, I did.

Q It is not normal to confirm orally, is it?

A It is not as common a practice as written confirmation, that is certainly true.

Q It is normal to confirm in writing?

A Yes. That would depend to some degree on circumstances in which people are involved in a particular audit. But that is true, it is more normal to confirm in writing.

Q Mr. Natelli, you knew that these particular so-called sales were not legal binding contracts, didn't you?

A I believe that we understood them to be commitments and there was a question as to whether they were legal binding contracts in the fullest form of that sense, yes, sir.

Q You said there was a question?

A I believe that is what I said.

Q Didn't you read what Mr. Scansaroli said here in Exhibit 3, his work papers, the very second page of the case you asked him to make for this group of contracts?

He said, "Under this method extra caution should be used because there is no legal binding contract."

Did you read that?

A I probably did at the time, yes, sir.

Q In fact, you understood throughout that these were not legal binding contracts, didn't you, sir?

A I understood that they were commitments and that the substance of what we were dealing with was that they were commitments from the clients to NSMC.

As to the question of legally binding commitments, I don't know that I had given a lot of thought to whether they were or were not, but I don't think that was an important part of the consideration.

Q You don't think that was an important part of the consideration?

A No.

Q I see.

A That I had at that time, that's right.

Q Later on you realized just how terribly important it was, didn't you?

A No, I don't think that is a fair way to put it. I did always realize that it was important that a company have good administrative procedures.

7A

Q Government's Exhibit 16 in evidence has been identified as partial notes taken by a stenographer at the meeting of June 9 between yourself and Mr. Randall. I am reading from the third page.

You told Mr. Randall on June 9, only about six or seven months after these contracts were booked, "$45 million in sales is fine, but it is important that 3.3 million is unbilled in the balance sheet. Suppose we do run into problems. Will you sue them? Doubt if you have a case. I've got to look at the negative."

You said that, didn't you, Mr. Natelli?

Q I don't know if I said that verbatim, but it is possible the sense of part of the discussion, yes, sir.

Q You don't deny that you said that in substance, do you?

A I can't deny it because I don't recall whether I did or didn't say it entirely in the way it is written there. But in substance I probably said something like that.

Q It is important, isn't it, that these things were not legally binding and could not be collected, isn't that correct?

A At that time that's I think got to be an inaccurate statement, although I don't remember the figures that you are referring to, because I believed at that time we did have

legally binding commitments on these items. There may have been a question that was being raised there as to whether or not the company would persue some of these items if they didn't go through because of their concerns in building a market relationship with these clients.

Q You aren't saying that the $1.7 million of contracts booked in October of 1968 with respect to those so-called sales -- that you actually got binding commitments, are you? You knew that you never got them.

A That's probably a fair statement.

Q Did Mr. Scansaroli tell you, sir, with respect to these not legally binding contracts the fact the salesmen hadn't even secured the business for sure? Did he tell you that?

A I don't recall that being said, no, sir.

Q Did Mr. Scansaroli ever tell you, sir, that he felt that with respect to these sales, so-called sales, the situation was touch and go?

A No, I don't recall him ever using such words at the time, no, sir.

Q If he had you would have remembered it, wouldn't you?

A I may or may not have. I can't speculate on that. I am simply telling you what I do or don't recollect

now, sir.

A Did he tell you that there was a concern that if the ad agencies were contacted they might in fact send the business to somebody else instead of to National Student Marketing?

A No, I don't recall that.

Q He didn't tell you that?

A I don't recall that he did tell me that, no.

Q Do you deny that he told you that?

A I don't recall that he told me that.

Q Would you remember a thing like that if he did?

A Probably so, but it would depend on the context in which it may have come up for discussion, if it came up. I simply do not recall him telling me that.

Q You heard Mr. Scansaroli testify here last week and he was read the material I have before me from his grand jury minutes with respect to that very language, touch and go and so on.

That came up, did it not, in the context of whether sales could be confirmed in writing or orally? Does that help you fix the context that it might have been in?

MR. MARTIN: I object to that, your Honor.

THE COURT: As a question designed to refresh his recollection I think it is permissible.

Q Does that refresh your recollection?

A I am afraid you will have to read it again.

Q What Mr. Scansaroli was telling to the grand jury was the reason for not confirming in writing, it was touch and go and so on, the advertising agency might send the business to somebody else, does that refresh your recollection as to whether Mr. Scansaroli ever told you the danger that National Student Marketing might not even have this business?

A That refreshes my recollection as to what was said the other day, but it does not bring to mind any such conversations at that time, no.

Q So that if Mr. Scansaroli knew it he just didn't clue you in, is that the idea?

MR. MARTIN: Object to the argument.

THE COURT: Sustained as to form.

Q In carrying out your responsibility for supervising the audit, Mr. Natelli, did you tell Mr. Scansaroli it was all right simply to assume the percentage of work done during the period under review?

A I don't recall using those words, no.

Q Do you recall telling him that in substance, with or without those particular words?

A I recall telling Mr. Scansaroli to follow certain

procedures which I believe I described here previously in order to attain some satisfaction as to the status of these contracts.

Q Did you tell him it was okay to simply assume that the figures he had been given by the company were figures as of August, which was the end of the period?

A Did I tell him to assume that?

Q Did you tell him it was okay to assume that?

A No, I don't recall a question ever coming up where I may have had the opportunity to tell him it was or wasn't okay to do that.

Q Do you recall if he ever told you that he simply just assumed that the work had been done in the period for which you were certifying financial statements?

A No, I don't recall him saying that.

Q If he told you something like that you would have remembered that, wouldn't you?

A Yes, I probably would have remembered it had he said it, yes, sir.

Q I believeyou have told us the big change that you made with respect to the previous unbilled accounts receivable reporting was to take percentage of completion instead of the whole contract, is that correct?

A I don't recall saying anything about a big change,

sir.

Q Do you recall telling the jury that the difference suggested by you or the system suggested by you might differ from the previous use of these contracts in that you were taking in a percentage of the contract rather than all of it?

A I believe I explained that that's what my understanding was as to what we did as compared to what we understood from Mr. Randall and Mr. Kurek had been done as of May 31, 1969. I believe that's correct, yes, sir.

Q Did you approve the recording of 100 per cent of the Schick contract of $30,000?

A I don't recall approving any particular contract individually.

Q Were you made aware of the fact that the Listerine contract in the amount of $70,200 was taken in as 100 per cent completed?

A No, but -- well, I will answer your question. No, I don't recall being made aware of it.

Q Were you made aware of the fact that the Ban contract in the amount of $19,500 was taken in as 100 per cent completed?

A No, I don't recall being aware of that. I may well have been. My answer should not be implied to mean that

I didn't know. I am saying I don't recall having been made specifically aware of any of these items.

Q It was not secret to you, sir, that at that point in time National Student Marketing hadn't done anything for any of those three clients for which they could bill one red cent? That's true, isn't it?

A It was not secret to me at that time. I wouldn't know whether I did or didn't know whether they could bill any amounts as of the time we were talking about. I don't know. I was not that familiar with the detail of what you are talking about.

Q I see. Didn't you review the schedule of this $1.7 million of sales that was being added two months after the period?

A I believe I reviewed it in general terms with Mr. Scansaroli, but not in any detail, that's right, sir.

Q You weren't interested in seeing if in fact what you had thought was going on was in fact going on with respect to this audit?

A I don't see how you can conclude that from what I just said, if that's what your question is.

Q Were you aware of the fact that in your supervision of this audit that Mr. Scansaroli had unwittingly talked to National Student Marketing's printer?

A I don't believe I was aware of the fact that Mr. Scansaroli may have talked to National Student Marketing's printer.

Q So you weren't aware of it?

A I don't believe so.

Q Did Mr. Scansaroli himself ever tell you that he didn't know who it was he was talking to?

A No, sir.

Q Did you know that the work papers failed to record in many instances who it was that he did talk to?

A I can't say that I had that specific a review of the work papers where I would have noted situations where he did or didn't record who it was he spoke to.

Q You did review these work papers though, didn't you?

A I believe that it is correct to say that I looked at them in the course of discussions with Joe Scansaroli, but not in detail.

Q But you didn't notice these things?

A I don't recall noticing them, no.

Q If you had noticed them you would remember it, wouldn't you?

A Today six years ago? I don't know.

Q It is not unusual, is it, to fail to record the name of a person contacted in your work papers when you are confirming, is it?

A That is such a broad question as to what is or isn't unusual. Obviously I would have to say it is not desirable, if that is what you are asking.

Q It is not desirable, is it?

Did you okay the practice of having the client dial the telephone for Mr. Scansaroli while he was confirming these $1.7 million of sales?

A I was never asked whether that could or couldn't be done and, no, I did not okay it because I was never asked the question.

Q You wouldn't have approved such a practice, would you?

A I don't know whether I would have or not. I don't see anything particularly wrong with it, instead of me dialing a number, I'm sitting there and I watch somebody else dial a number. It's never been a question I had to think much about.

Q Did you notice he wrote down the numbers which were being dialed?

A Did I notice that he did?

Q Or didn't.

A I don't know particularly that I did or didn't

Q He didn't, did he?

A I don't know.

Q Do you want to check?

A I really don't see what importance it has. If you want me to check, I will check, to answer your question.

Q Please. Why don't you try page 1970 and any place else you care to look.

(Pause.)

A I don't see anything that indicates telephone numbers no, sir.

Q I see.

In fact, in the succeeding years' audit, the 1969 audit, you were still in charge of the audit then, weren't you?

A Yes, I was.

Q Because there had been problems with the unbilled accounts receivable in '68, you recommended a better procedure, didn't you?

A I recommended a procedure in 1969 which was different from '68 yes, sir.

Q Incidentally, the '69 audit was completed after the proxy statement, isn't that correct?

A That's correct.

Q And in the '69 audit there was written confirmation, wasn't there?

A Yes, there was.

Q You heard Mr. Johnston say that he kept direct control of those confirmations, making sure that nobody touched them but Peat, Marwick personnel until they were mailed, is that correct?

A That's correct.

Q Making sure they came back to him in self-addressed mailers, is that correct?

A That's correct.

Q He confirmed all of them?

A He said he sent confirmations out on all of them at my direction, yes, sir.

Q Positive confirmations?

A Yes, sir.

Q Carrying out your responsibilities and supervising the 1968 audit -- you knew how to do all of those things in 1968, didn't you?

A Yes, sir.

Q You chose not to?

A I chose not to? In the circumstances, that is correct.

Q Okay. In carrying out your responsibility for

supervising the 1968 audit, did it come to your attention that National Student Marketing was making money back guarantees with respect to some of these so-called sales?

A No, it did not.

Q Mr. Scansaroli didn't tell you that, did he?

A I don't recall him telling me that, no.

Q You would have recalled that if he told you, wouldn't you?

A Probably so.

Q Didn't you read the commitment letter from Syntex which resulted in $138,000 sale?

A I don't recall that I read that letter, no.

Q It was right there in the work papers, isn't that right?

A Yes, it is.

Q Tell us, Mr. Natelli, what was your understanding of what exactly National Student Marketing had done to warrant or justify recording half a million dollars as earnings in 1968?

A My understanding was that they had developed during the year a program which was described as fixed fee type programs in which account executives that they had brought into NSM during the year went out to National companies and designed programs, consulted with them, if you will.

on programs to reach the youth market, essentially the college market, with information about companies or their products either services or products.

Q You understood that that's what they had done and was worth half a million dollars, is that the idea? They had earned half amillion dollars back there in 1968 for that?

A I understood that's what their activity was and that that is what we were accounting for, yes, sir.

Q Did you know whether Mr. Scansaroli ever checked to see if they ever did any such thing?

A I believe that he did in the course of his work have reason to believe that they did such things, yes, sir.

Q Did he ever show you a program booklet like that Eastern one, lots of nice prose in it about the company and so on?

A I don't recall him showing me one, no, sir.

Q There's none in the work papers, is there?

A No, not that I know of. There may be. I don't know of any.

Q Take a look. It is right in front of you.

A I don't see any in here, no, sir.

Q So you never laid your own eyes on that 85 percent

completed half a million dollar item, did you?

A Did I ever lay my own eyes on it?

Q Yes. Did you ever look at it?

A I don't know how I can answer that question.

Q Did you ever look at a program booklet for Clairol?

A No, sir.

Q As far as you know, Mr. Scansaroli never did either?

A I don't know that he did or didn't. I don't know.

Q It wouldn't have been that hard up there at the National Student Marketing office just to see if they had a program booklet, would it?

A I'm sorry, I don't understand your question.

MR. MARTIN: I object, your Honor, as argumentative.

THE COURT: He doesn't understand the question. I'm going to ask him, therefore, to rephrase the question.

Q Assuming that National Student Marketing had, in fact, made up a booklet, they probably would have kept one in their files, wouldn't they?

MR. MARTIN: I object, your Honor.

THE COURT: Overruled.

A I presume if they had made one up, they would have kept one in their files.

Q It would have been available to look at it?

A To whom, to me?

Q To you or to Mr. Scansaroli or Peat, Marwick and Mitchell.

A I presume if they were there in their files, Mr. Scansaroli might have been given the opportunity to look at them, yes, sir.

Q Mr. Scansaroli never told you he did any such thing, did he?

A I don't recall him telling me that he did. I don't recall him telling me that he didn't either.

Q I see.

Mr. Kurek told you in December, early December 1968, that he hadn't received any contracts yet on these large commitments, did he?

A I don't recall any particular discussion with Mr. Kurek in early December to that effect, no, sir.

Q Is it your testimony that you heard absolutely nothing unsettling or disturbing about these contracts between when they were booked at the end of October and December?

A I think that Mr. Kurek had indicated to me -- I can't give you exact dates, but Mr. Kurek had indicated to me on occasion that he was having difficulty in getting the

administration of these contracts under control, yes, sir.

Q You say, "administration of these contracts".

That means getting a contract out of the clients, doesn't it?

A No, that's not necessarily what I mean. It means getting information from the account executives as to where the status of these contracts were.

Q The status of the contracts in virtually every last one of them the next thing to do was to get a contract, wasn't it?

A I'm not sure about that.

Q You are not sure.

Tell us, did any unsettling news with respect to whether these contracts had yet been obtained come your way before December?

A Not that I can recall, no, sir.

Q You heard Mr. Kurek testify that on the day that you had the meeting, December 9, 1968, thereabouts, he spoke to you on the telephone and toldyou that the account executives had reported they hadn't received contracts yet and he hadn't even heard from some of the account executives.

That was the truth, wasn't it?

A I really don't recall that. I heard him say it, but I don't recall a phone call from Mr. Kurek and I don't

recall a meeting on that day taking effect as a result of his phone call which is what he said.

Q You told us that that meeting was a so-called exit interview, is that correct?

A That kind of a meeting, yes, sir.

Q So without having heard any bad news about these contracts, you just on your own told him" "From now on, fellows, it is going to be written contracts, no more oral ones," is that what you said?

A Well, I think you are making a little jump there. I think the fact is that while we had to deal with the situation that we found when we came into the company, and this is what I believe we did say at that meeting, that on a prospective basis we had to recommend that the company become involved in obtaining written commitments.

Q What ~~made~~ came up that all of a sudden they needed written commitments ~~from~~ when the oral commitments had been satisfactory enough to book $1.7 million of them only two months before?

A I don't think I ever said it became anything that I did think was necessary allof a sudden, Mr. Velie. Those are your words.

Q Why did you change the signals from oral contracts to signed contracts over that two-month period?

A I didn't change any signals as to what I thought was the appropriatemethod of administration for these kinds of items.

Q Let's get it nailed down here.

In October you permitted them to book 1.7 million of so-called sales, all of which were oral except for Syntex and one or two other minor ones, is that correct?

A That's correct. As I understand it, most of their contracts at that time were oral, yes, sir.

Q You have told this jury that only two months later in December you told National Student Marketing we are going to have to have written contracts.

A That's correct.

Q Did something happen in between those two events which called to your attention the fact that there was a real problem with oral commitments?

A Not that I can recall, no.

Q I see.

In fact, Mr. Natelli, are you quite sure that in December you told them you wanted written contracts?

A Am I sure?

Q Yes, sir. You have testified to it. I am asking you if you are sure that is what happened.

A Yes.

Q I show you Government Exhibit 7. It has been identified, has it not, as Mr. Kurek's memorandum of the December 9 meeting which you told us about, isn't that correct

A Yes, sir.

Q Mr. Kurek made that memorandum the very day after that particular meeting, didn't he?

A Apparently so.

Q December 10th?

A Yes, sir.

Q And he said in there, "That what you said was that by August 31, 1969 they", Peat, Marwick, Mitchell, "wanted all contracts or commitments to be firm enough for them to be able to send written confirmation to the clients."

That is what he wrote down, didn't he, the very next day?

A Yes.

Q He didn't write anything down about having to

get written contracts thereafter, did he?

A I don't believe that he did in this particular memo, no, sir.

Q So you are saying that your memory of this event all these years later is better than Mr. Kurek's the next day, is that what you are telling us?

MR. MARTIN: Objection. It is argumentative, your Honor.

THE COURT: Overruled.

A I am telling you that my recollection is that at that meeting it was agreed that on a prospective basis the company would obtain written commitments. Yes, sir, that is what I am telling you. As to what Mr. Kurek may or may not have written, I am not in a position to answer for his words. On the other hand it is true that with respect to Peat, Marwick's view of the situationas the outside auditors, certainly the emphasis of the discussion would have been in the light of what we came in and found as of a certain date and recommendations to the company as to what we wanted them to do to improve their administration, looking ahead towards the next date at which we would probably have some responsibility with them; yes, that is the context of it.

MR. VELIE: Would you please read the question

for Mr. Natelli to answer.

(Question read.)

Q Is that what you are telling us, Mr. Natelli?

MR. MARTIN: I think he has answered the question, your Honor.

MR. VELIE: No, he didn't.

THE COURT: We will let the jury decide. You gentlemen have both made comments. Do you want this question answered again or not?

Q Why don't you try again. Do you understand the question?

A I would say that my present recollection is what I can best recall as happening, yes, sir.

Q Doyou recall telling the jury that you had a hazy ~~hazy~~ recollection of part of that particular meeting?

A Do I recall telling the jury that?

Q Yes.

A I am not sure -- no, I am not sure that I did tell them that. I believe that is probably correct.

Q Why don't you take a look at Page 1846 of the transcript. I have underlined it for you. You did tell the jury, didn't you, that you had a hazy recollection with at least one aspect of this meeting?

MR. MARTIN: Your Honor, I object. That is

unfair to give him what appears on that page.

THE COURT: Since I don't know what page it is, I am unable to comment.

THE WITNESS: Would you like to look at it, your Honor?

THE COURT: Thank you.

(Pause.)

THE COURT: I am not even certain what you are trying to get at. I think perhaps the objection is well taken at least to this extent. Why don't you read and ask him whether or not he recalls stating whatever it is you want him to focus on.

MR. VELIE: Sure.

Q You were asked who attended the meeting, and you answered, "I can specifically recall Bernard Kurek, Cortes Randall, Joe Scansaroli and I being present. I seemed to have a hazy recollection. There may have been other individuals in the room during the meeting, but I am not sure who they were."

Your recollection of who was there is hazy at this meeting, is that correct?

A That's correct.

Q But you are positive that you said they had to have written contracts from then on at that particular meeting

A Yes, I am, sir.

Q In May of 1969, five months later, you knew that three-quarters of a million dollars of those contracts had been written off, didn't you?

A Those are the Ron Michaels contracts I believe you are referring to, sir?

Q Yes.

A Yes.

Q Shortly after May, in June, you learned that, in fact, about a million dollars of contracts had been written off by the company, is that correct?

A I believe that is correct, yes, sir.

Q That is, a million dollars of the 1.7 million that you had booked approximately six or seven months before, is that correct?

A Yes, that is what it turned out to be.

Q You had audited those very contracts, sir, supervised the audit, is that the idea?

A Yes,sir.

Q Did you then check to see if there had been something insufficient with respect to the audit that you had supervised?

A No, I did not.

Q Did you check to see if the balance, the $700,000

in contracts, should be written off also?

A Well, I believe in connection with the work that we did on the proxy, in following our review procedures, we asked the company to make that determination, yes.

Q And you found that several other large commitments were also worthless, didn't you?

A I believe there has been testimony here as to what took place regarding that review which pertains to the work that Mr. Oberlander did and Mr. Scansaroli's meetings with Mr. Kurek regarding those items, yes, sir.

Q I am talking about Mr.Scansaroli's May review prior to June. Mr.Scansaroli had made findings with respect to the Barnes-Hind commitment in the amount of 22,400, Campana in the amount of 21,900, Faberge in the amount of 53,775, Gossard in the amount of 3775, Pace in the amount of 14,492, Carnation in the amount of 11,200.

On May 22 he found that all of those were highly suspect. Didn't he tell you about it?

A I don't recall having discussion about those items with Mr.Scansaroli, no.

Q It is right in the work papers. Didn't you take a look at the SEC review portion of your proxy?

A No, I did not.

Q In fact, you had your own suspicions, didn't you,

about these particular contracts?

A Not that I can recall because I don't recall that I knew about any of these specific contracts in detail. I don't know.

Q About all of the contracts, the 1.7 million, you had become highly suspicious, had you not, that all of those contracts were non-existent or worthless?

A No, I don't think so. I believe that I was very much concerned over the information that I did have, which was that we did have the Ron Michaels contracts which fell apart and other items that had been written off by the company, but mainly about the fact that the company on a prospective basis should do what we had agreed they would do with respect to written statements. That is what my concern was, as I recall it.

Q Let me just see if I have it right.

You were concerned, is that correct?

A Sure. Of course I was concerned.

Q Were you concerned that people might be relying on the annual report for 1968, which was then only four or five months old, in relying on the fact that the company had $1.7 million worth of sales when you knew that those sales didn't exist? Weren't you concerned about that, sir?

A I don't recall that I had concern about the 1968

report at that time. Frankly, I have no recollection of being concerned about it. The company was quite changed in the interim already at the time that we are speaking of here.

Q How did it change?

A How did it change?

Q Yes, sir.

A There were a number of companies that had become part of NSMC.

Q They had been acquired for National Student Marketing's stock in whole or in part, is that correct?

A I believe in some cases they were, in other cases they were acquired for cash and notes, yes, sir.

Q Those that had been acquired for stock had, as their latest information to know whether to be acquired or not, that annual report which showed $1.7 million of unbilled accounts receivable sales, isn't that right?

A They would have had, yes, sir.

Q So the company changed by acquiring people who had been relying on your report, that's true, isn't it?

A To the extent that they would have read that report and relied on it, which I don't know that they did or didn't do, that would be true.

Q If they did they would have been cheated, woujldn't they?

MR. STILLMAN: Oh, your Honor --

THE COURT: Sustained as to form.

Q Let's just see. If they read that report they would have thought that the company had sales of $5 million of which $1.7 million were these unbilled accounts receivable, isn't that right?

A Yes, sir.

Q In fact --

MR. MARTIN: Objection as being argumentative, your Honor.

THE COURT: Overruled.

MR. MARTIN: We are talking about the state of somebody else's mind.

MR. VELIE: We are talking about the state of Mr. Natelli's mind.

Q You knew, didn't you, that there were no such sales of $1.7 million and there were no earnings regarding that as part of National Student Marketing?

A Now we are talking about the May period, sir?

Q Yes, May and June.

A May and June I knew that there were contracts that had to be written off, some of which were written off

retroactively, having, in the case of the Ron Michaels contracts, an effect on gross profit of approximately $200,000 and in that time frame we also knew that there was a tax error which had an effect -- a contrary effect of approximately $190,000, and that there was a net effect at that point of about $21,000 on the net earnings. Yes, I did know that, sir.

Q So you didn't think, did you, that it would be worthwhile telling the people who had given up their companies in exchange for National Student Marketing stock those sales didn't exist after all?

A I don't think that I ever reflected on that, no, sir.

Q Did you know that what the company had done was to put these sales on and replace them with the sales and earnings of the companies they were gobbling up?

A Did I know that they were putting these sales on and replacing them? I don't know how to answer that question, frankly.

Q Did you know that the company had in fact booked a lot of sales, acquired other companies which had sales and earnings, and then quietly wrote off the sales which the company had originally put on?

A Once again, as to information that I knew, I

certainly knew that companies had become part of NSM and were being accounted for, if they were pooled companies, as part of NSM, if they were purchased companies, then they were not being so reported, and I did know the extent of the contract problem as we just described previously, that there was a net effect of $21,000 on the net earnings.

Yes, I knew that information.

Q To say the least, Mr. Natelli, this annual report, Government Exhibit 5, was inaccurate, wasn't it, it didn't tell the truth about National Student Marketing?

MR. MARTIN: Objection, your Honor.

Can we fix a time?

Q Did it ever tell the truth?

THE COURT: Just a moment. One thing at a time, please. I will sustain theobjection to this extent. I assume that you want to put this in a given time period.

MR. VELIE: I will do that, your Honor.

THE COURT: Did there come a time.

Q In June of 1969, you knew that that report was inaccurate to the extent that it reflected $1.7 million of unbilled account receivables, isn't that correct?

A In June of 1969 I knew that the report that had been issued by National Student Marketing Corporation as of 8/31/68 had to be adjusted with respect to the sales that

we have discussed but that it also had to be adjusted at that point in time to take into account whatever would have taken place from that time in the way of companies acquired, yes, sir.

Q Let's just take it one piece at a time.

You knew that the information in there about unbilled accounts receivable just wasn't true any more, didn't you?

A It turned out that some of those contracts had to be written off, yes, sir.

Q Some of those contracts? $1 million were written off by June, and you knew it?

A A portion of which were written off in 1969, a portion of which were written off in 1968, yes.

Q The fact was that they were written off because they were worthless and no good, isn't that correct?

A They were written off in one case because, as I understood it, they were determined never to have been in existence, and --

Q What about the other one-quarter of a million dollars of sales? They were written off too, weren't they?

A Yes, they were.

Q Those weren't good sales?

A I believe they were written off because it turned

out the clients did not wish to go through with the programs at that particular time or reasons of that nature.

Q But they were written off because the company in fact didn't earn a quarter of a million dollars the way you said that they had, is that correct?

MR. MARTIN: Objection, as argumentative, your Honor.

THE COURT: Yes. "The way you said that they had," is susceptible of a number of interpretations.

Reframe it.

d 9A

Q The fact is the company didn't have a quarter of a million dollars of sales which you had reported as being sales in that annual report.

A The company did not have as sales a quarter of a million dollars? I am sorry, but you have lost me. Are you talking about the gross profit on certain contracts?

Q No. There was another quarter of a million dollars in sales written off, taken right out, isn't that correct, Mr. Natelli?

A In 1969?

Q Yes.

A Yes, sir.

Q You knew about it in June?

A Yes, sir.

Q So that the report was inaccurate to the extent of another quarter of a million dollars, is that correct?

A I wouldn't agree as an accountant that that has the implication thatyou are trying to draw with respect to those figures.

I will agree that a quarter of a million dollars of contracts that had been recorded by the company at 8-31-68 were subsequently written off in 1969.

Yes, I will agree with that.

Q That plus the $750,000 means $1 million of con-

tracts had been written off, is that correct?

A Yes, you have added thatup many times, yes, sir.

Q On June 9 you had a meeting with Mr. Randall. You remember that?

A Yes, I do.

Q Mr. Kurek was also there and some other people?

A Yes, sir.

Q You heard Mr. Kurek testify about it?

A Quite frankly, I believe he did. At the moment I can't remember what he said. But yes.

Q You remember Government's Exhibit 16, his notes of that? We have shown them to you already this morning.

A Yes. I don't think you showed them to me, but I know what they are, yes, sir.

Q At thatpoint in June there was no question in your mind that $3.3 million of unbilled accounts receivable had thus far been booked, is that correct?

A If that's what the indication there is in those minutes, I must have had recollection. I don't think the number would have come from out of the air. But on the other hand, it is not a verbatim transcript, so I don't know.

Q Take a look at that number right there. Does that show $3.3 million?

A This shows next to Cortes Randall's name that --

there are some notations here that he apparently said something of that nature, yes, sir.

Q The fact is that there were $3.3 million worth of unbilled accounts receivable sales, the grand total booked in the first six months of 1969, plus those that had already been booked for the year ended 1968, isn't that true?

A I believe that's correct from information that we have, yes, sir.

Q In fact, they had all been booked during the period between October, when you added the 1.7 million in, and June? That's correct, isn't it?

A It would probably have to be correct, in that time frame, yes, sir.

Q There was discussion at that meeting about the fact that approximately $1 million of those sales had already been written off, is that correct?

A Of which sales now, sir? I'm sorry.

Q These are the '68 sales. Almost $1 million of the '68 sales were discussed as having been written off at that meeting?

A You are going back to '68 sales again?

Q Right.

A I believe there was discussion of the fact, yes, sir, that there was -- that there were contracts written

off that had been booked in 1968.

Q $1 million of them?

A Once again, $1 million.

Q Did you say that in addition $800,000 of the August 31, 1968 figures did not come through?

MR. MARTIN: Objection. Is this in addition to the 1 million?

A I am thoroughly confused now, Mr. Velie. I don't know.

Q Just take a look at these two lines. First of all, Mr. Randall used the figure 978,000 instead of 1 million, didn't he? Is that correct?

A Yes, it appears that he is using 978,000.

Q He says 978,000 of the contracts have been written off, is that correct?

A Yes.

Q You say just a line below that $800,000 of the August figures didnot come through. Did you say that?

A I can't say that I specifically recall making that statement. That's what is indicated there in those notes, yes, sir.

Q So that if the secretary wrote this down perhaps she made a mistake?

A I really can't say. I don't know.

Q Do you deny saying that $800,000 of the August figures did not come through? I am quoting, "Did not come through."

A I may have said it. I don't know. But that apparently would refer to probably the Ron Michaels contracts. I don't know.

Q If you add together the 978,000 which were written off and the 800,000 which didn't come through that is $1.7 million, the total of the 1968 sales, isn't it?

MR. MARTIN: I object. It is taking two remarks out of context. If he wants to read the document I have no objection to it.

MR. VELIE: We have a witness here who said these things.

THE COURT: The jury will decide that. The objection is overruled. He is simply going through the addition, as I see it.

THE WITNESS: I can't say that, your Honor. I don't know that the conclusion that he is drawing is an appropriate conclusion between a statement that Mr. Randall may have made and a statement that I may have made.

THE COURT: All right. We will suspend now for luncheon, ladies and gentlemen of the jury, and we will resume promptly at 2:15.

(Luncheon recess.)

AFTERNOON SESSION

2:15 p.m.

xx A N T H O N Y M. N A T E L L I, resumed.

xx CONTINUED CROSS EXAMINATION

BY MR. VELIE:

(In open court, jury present.)

THE COURT: Mr. Velie.

MR. VELIE: Thank you, your Honor.

Q Mr. Natelli, prior to lunch, we were talking about the meeting of June 9, 1969 and you had given us your explanation of Mr. Randall's remark about $978,000 of 1968 contracts having been written off and your explanation of your remark that $800,000 out of the August figures did not come through.

Do you recall that?

A I recall that being a subject of discussion, yes.

Q Do you recall pointing out to Mr. Randall the fact that 3.3 million dollars of unbilled accounts receivable, to use your phrase, were sitting unbilled?

A I can't say that I presently recall doing that, but I know it is an item in those minutes, yes.

Q You don't dispute that it is right here in Government's Exhibit 16 in evidence attributed to you?

A I have no reason to dispute it, no.

Q Do you deny you said it?

A No.

Q You just don't remember?

A I don't recall, that's right.

Q Well, do you recall telling Mr. Randall that the total volume of sales for 1969 has yet to be performed, they are all sitting unbilled? Did you say that?

A Once again, I can't recall saying it, but I think the point of emphasis at that whole meeting was in my area of concern as to this particular topic, yés.

Q Why don't you just read -- I will read it to you. This is in evidence.

"Tony"-- and it quotes you as follows, "Total volume of sales for '69 has yet to be performed. All sitting and unbilled."

Does that refresh your recollection as to whether or not you said that to Mr. Randall?

A It doesn't refresh my recollection as to whether I said it. I'm not even sure at the moment that that is necessarily correct or not. I don't know.

Q You told us that you recall that there was a secretary there taking notes?

A Yes.

Q Shorthand notes?

A I don't know if she was taking shorthand, long hand or speedwriting, sir.

Q Well, do you recall saying that "It is important that 3.3 million is sitting unbilled in the balance sheet?" Do you remember saying something like that?

A I'm sure that I was emphasizing my concern over the unbilled receivables because of my concern, especially with the Pontiac letter, yes, sir.

Q In fact, it is important that the company just had them sitting there unbilled on the balance sheet, wasn't it?

A Was it important that they were just sitting there unbilled?

Q Yes, sir.

A It was important if they were sitting there unbilled in my concern over, in particular, the element that represented the Pontiac commitment letter, yes, sir.

Q You knew the problem wasn't just Pontiac, didn't you?

A I had concerns over the whole situation, yes, sir.

Q The whole situation. You knew the problem wasn't just Ron Michaels either, didn't you?

A I knew the elements of the problem at that time being the Ron Michaels contracts, the additional couple of

hundred thousand dollars that the company had to write off and the Pontiac item. I think that's a fair summation of what my concerns were, yes, sir.

Q Weren't you concerned about the new sales which were just sitting unbilled in 1969 sales recently booked and they are just sitting there unbilled, to?

A I don't really believe so.

Q You weren't concerned? Well, wasn't that what you were referring to when you said "Total volume of sales for '69 has yet to be performed and they are all sitting unbilled?

A I don't really recall once again that particular comment, but anyone reading those notes and gaining the substance of that meeting, it was my concern over looking ahead to 8-31-69 and being sure that the company was going to be dealing with these fixed fee contracts in the way that we had agreed they would be dealt with, sir.

Q Wasn't it your concern that they had stuck all this stuff into their reports, 3.3 million bucks work of it, and thatif there was a problem, they couldn't recover one red penny?

A My concern was over what I would be responsible for with respect to this company at the next instant of what I thought knew would be my responsibility, which was with the 8-31-69 audit, and it is obvious from a reading of those notes such

as they are, as partial as they are, that that is what the meeting was about.

MR. VELIE: May I have the question read back, please.

(Question read.)

Q Would you please answer my question, Mr. Natelli?

A My concern was that they had items in their unaudited statements for which I did not have a responsibility, which were there in a manner that was not in agreement with what we had agreed would be the procedure for these contracts. That's right.

Q Was it, sir, your concern that they couldn't ever get those earnings despite the fact that they had already reported them as earnings?

A No, sir.

Q Didn't you say, "Suppose we run into problems, will you sue them? Doubt if you have a case? I've got to look at the negative"? Didn't you say that?

A As I have previously mentioned, I had made -- I had made a number of comments in that meeting that were to be sure that they understood my concern, and I think I also said that I probably exaggerated certain comments in order to make sure they are aware how serious I was, that I wanted them to do what we had agreed upon between the company and

Peat, Marwick as to how this business would be handled and recorded on the books.

MR. VELIE: Would you please read Mr. Natelli the question.

(Question read.)

Q Is that something you said?

A I'm not sure that I said what that represents in those exact words.

Q Do you deny saying something like this?

A Something like that? I don't deny that I may have said something like that, no, Mr. Velie.

Q That is the substance of it, you were concerned that they would never recover one cent on these earnings?

A That's not the substance of it. The substance of it, I was concerned that they would be recording items on the books that I felt they should not be reporting on the books as of yet; for example, the Pontiac letter, and I wanted to be sure that as of 8/31/69, we were at , in a position where we were expecting to be.

Q I just want to ask you: Do you deny saying what is attributed to you here on this exhibit in evidence, "Suppose we do run into problems, will you sue them? Doubt if you have a case, I have got to look at the negative,"? Do you deny having said that?

MR. MARTIN: Don't you think we should have the fact that the document itself indicates there are gaps in between some of those words?

Q Do you deny having said that?

A I am just not sure that I said those words the way they are prepared there.

Q Do you recall what you did say?

A No. I think I may have said that there was some question as to whether they would pursue these because I knew that one of their concerns was to be building this kind of business activity with the clients that

they were dealing with. We did have some examples of some of the items that were written off in '69, as I understand it, being such type items, that the client decided they didn't want to pursue it yet, they were going to push it off into another period and the company, that is NSM, didn't want to push the client and say you said we are going to do this, why don't you come ahead and come through with it. They wanted to keep the client relationship. I did make a comment along those lines. I don't recall making the comment in complete fashion that you have there or partial fashion, whichever way you want to look at it.

Q Just so there is no confusion about this, if, in fact, you said what you just said you said, then the notes are wrong, aren't they?

A Are they wrong?

Q Yes, sir.

A I have never -- I have never taken a position as to whether they are wrong or right in detail, sir.

Q Take a position.

Is that entry wrong or is it right with respect to what you said?

A I am just not sure.

Q I see. Do you recall telling Mr. Randall your concern regarding the six month figures, that is the first

half of 1969, and later two more contracts came into the figures after the period had closed?

A I can't recall what specific items they might have been. I know that it is in there and I believe that I did mention something about the problem of the cutoff, once again, the cutoff on when these were recorded. I think one of them was the Pontiac letter.

Q In fact, Pontiac was a post period adjustment, isn't that right?

A I believe that it was. I am not sure of that. I believe it was though from more recent review of documents, yes.

Q There is no question that the Pontiac ~~equipment~~ commitment letter is dated April 28, is there?

A Yes, that's right. You are right.

Q And the period closed in February, two months before that?

A Correct.

Q Right.

A You are absolutely right.

Q Once again the company had jacked up its earnings after the period had closed by sticking in over a million dollars in sales, is that correct?

A They are unaudited figures, apparently so.

Q Do you recall telling Mr. Randall at that particular meeting the bigger a company is, the more susceptible they are?

A Once again, I can't say that I remember the exact words. I remember trying to impress upon them that they were a growing company, it was a big company and I wanted to be sure that they undertook their responsibilities to account for everything appropriately in the administrative area, yes, sir.

Q The bigger a company gets, the more susceptible they are, that is attributed to you.

Does that refresh your recollection that you said that very thing?

A I may have. I am not denying that I may have said it. There are also some dashes in there. I am not sure what took place in between those dashes. It is obvious whoever wrote these numbers was taking parts of what they heard. I can't deny I said it.

Q Mr. Natelli, there are no dashes in the sentence I read you.

A I am sorry, there are periods or something.

Q It says from where I start, "The bigger the company gets, the more susceptible they are." That is a complete sentence without any ellipsis dots, isn't it?

A I don't know what an ellipsis dot is.

Q Nothing left out of that sentence, that is a complete sentence.

A I guess grammatically that is correct.

Q Okay. You meant the bigger a company gets, the more susceptible they are to investigation by the Securities and Exchange Commission, didn't you?

A No, I didn't.

Q What did you mean by susceptible?

A As I said, I am not sure that I used that word. What I was concerned about was the company's method of recording its income and its procedures. That is what I was there concerned about. That is pretty obvious from a reading of the whole sentence of that thing. I can't help what it is that you would like to try and read into it. I am trying to remember what the substance of that meeting was.

Q Mr. Natelli, I am going to call your attention to the meeting of June 3 that you had with Mr. Kurek. Do you recall Mr. Kurek testified about that? You recall, of course, that Government Exhibit 14 in evidence is a memorandum written by Mr. Kurek the very day he met with you, June 3, 1969? That is so, isn't it?

A I believe that is correct, yes.

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Q In fact, it starts out "I met with Tony this morning from 9:30 to 11:00." Isn't that how it starts out?

A Yes.

Q Mr. Kurek reports in the memorandum he wrote that very day after your conversation that you, Mr. Natelli, he says, "now sees the situation as one where commitments either make or break us."

Did you say that to Mr. Kurek?

A I am not sure whether I did or not. I probably said that I could see a situation where the matters of unbilled receivables, if not properly handled, could make or break the company, or some such thing. I may have. I don't know. I think those are his interpretations of what I said. I don't know if I used those words.

Q Do you deny that you told him that the matter was one so important, the size of these contracts so large compared to the rest of the results of National Student Marketing, that the contracts in fact are the difference between making and breaking the company?

A I don't -- I can't say that I did not say that, to answer your question. I am not sure whether I used those words or whether they are his interpretation of my very deep concern -- you are quite correct -- my very

deep concern over this area of activity at that time.

Q Did you tell him that you had anticipated that the company would be selling and delivering on contracts in the same quarter that financial reports were made?

A I don't see how I possibly could have told him that. That has to be his interpretation and it just -- you know, it just has to be in error. If that were true, if that was what my expectation was, there would be no reason to even consider this accounting problem.

Q Did you complain --

A So it must be his interpretation, however much in error it may have been, of something that I said.

Q Did you complain to Mr. Kurek that the company was not performing in the period the sale was made?

A As a complaint?

Q Yes. Did you say it at all?

A I don't see how I could have.

Q I see.

A Not in terms of what you are reading there, because once again, if -- in the sense of performing, if the complete elements of these fixed fee commitments, these contracts, were being completed within a short period of time in the full sense of what you are portraying there there wouldn't be an accounting problem to have dealt with in the

first place.

Q In fact, the company was not performing on these contracts in a short period of time at all? That is fair to say?

A In a short period of time, no.

Q In fact, they weren't performing on them at all, were they?

A That is not true at all.

Q I see. You say that the company was performing on these contracts?

A So far as I knew, yes, sir.

Q You knew that $1 million of the 1.7 million had been written off?

A Yes.

Q You had said that $800,000 did not come through?

A I think you are talking about the same item now, Mr.Velie.

Q You had said that they are sitting unbilled, is that correct?

A I had said that there were some items sitting unbilled as described in the balance sheet. yes,sir.

Q You said,"Suppose we run into problems. Can you sue them? Doubt if you have a case." You said that?

MR. STILLMAN: Repetition,your Honor. We have

been through that.

MR. VELIE: Somebody seems to have changed the story.

MR. STILLMAN: I object tothat.

THE COURT: Yes, that will be disregarded. I do agree, Mr. Velie, that this has been covered before.

Sustained.

MR. VELIE: Very well.

Q Mr. Kurek wrote down in his memorandum of June 3 that you stated that the people working under you are uncomfortable with this situation and if anything were to happen their certificates and their careers would be at stake. That is the truth of the matter, isn't it, Mr. Natelli, that is what you told Mr. Kurek?

A I don't recall ever having used words of that nature.

Q Do you deny saying that to Mr. Kurek?

A I deny in the sense that I don't recall ever having used words of the nature that he has there.

Q You tell me. What was it that you told Mr. Kurek, if you recall, about certificates and so on?

A I don't really recall the question of certificat coming up at that meeting. I do recall, as I believe I have testified previously, that in the course of discussions

with Mr. Kurek about this time and my concerns about what they were doing there was a discussion about the company feeling that I was being unfair in not giving a fair hearing, if you will, to some of the things that they wanted to do, and I was concerned about the Pontiac contract being something that they put into their accounts at a time that I didn't think it was appropriate to put it into their accounts, and I did tell you also that there was discussion at that time that if he felt that I was being unfair they could get another accounting firm in.

Now, I think perhaps in the course of that discussion there may have been some mention about -- some philosophical discussion about the difference between a company's unaudited figures and what accountants' responsibilities were, looking ahead to the 8/31/69 audit, which was my concern.

Q Somehow or other Mr. Kurek when he wrote down this memo on the very day you spoke with him didn't record it that way, he recorded it this way, didn't he?

A As I say, I don't recall having used the words that he has portrayed there.

Q All right.

A And I also -- as I have previously said, I can't think of a specific meeting in which everything he has

portrayed there may have taken place. I do recall having meetings with Mr. Kurek at that time.

Q Pretty strong language, isn't it,about accountants losing their certificates and their careers being at stake?

MR. MARTIN: Objection as argumentative, your Honor.

THE COURT: Overruled.

Q Is that strong language, sir?

A Is it?

Q Yes.

A Yes.

Q Do you deny that you said that to Mr. Kurek?

A I deny that I said to Mr.Kurek that there was any concern by anybody with respect to losing their certificates,yes, sir.

Q You do deny it?

A Yes.

Q I see. Mr. Natelli, to say the least,it is professionally embarrasing, isn't it, to have to write off $1 million of commitments which you had audited?

A To say the least? I guess that would be fair to say, that it is embarrassing to ever have any errors come up, yes, sir.

Q You were embarrassed, weren't you?

A In a professional sense?

Q Yes, in a professional sense.

A I am a human being and we were doing a job and when problems came up that turn out to be errors in something we had done, of course there is some professional embarrassment.

Q Were you worried about the effect of this on your friend Joe Scansaroli?

A Absolutely not.

Q You were not?

A No.

Q Do you deny that you referred to Mr.Scansaroli as being a person who might have a problem if this ever came out?

A Did I ever refer to Mr.Scansaroli that way?

Q Yes.

A I have no recollection of ever referring to Mr.Scansaroli that way.

End 2A

Q Let me just see. You have denied making the statement here that people working under you are uncomfortable with the situation and if anything were to happen their certificates would be at stake? Is that your position?

A Now, wait a minute.

Q Have you denied saying that?

A I believe I denied saying that anyone working under me was concerned about losing his certificate. I did say that.

Q Okay.

A I don't know about the words that are used in that letter. I don't recall using those words.

I am not sure we are talking about the same thing here, Mr. Velie. You are taking what I say and then you are referring back to Mr. Kurek's words in his letter and I am getting a bit confused at this point.

Q Let's just get it as squared away as we can. I am going to read you this sentence and you just tell this jury whether you ever said anything of the kind to Mr. Kurek on June 3 as he notes that you did.

"He," meaning you, "stated that people working under him are ~~uncomfortable~~ Uncomfortable with this situation and if anything were to happen their certificates and careers would be at stake."

Now, did you or didn't you say this to Mr. Kurek,

as he noted that you did?

A I don't recall using those words to Mr. Kurek, and I would point out that I don't see any quotes, as you said there were quotes there, sir.

Q You see quotes around the words "certificates"?

A Yes, I do.

Q Does it say "He stated", meaning you stated?

A That's what it says.

Q Have I quoted this sentence accurately?

A I believe so.

Q You heard Mr. Scansaroli testify to this question by Mr. Stillman?

"Q To the best of your recollection, sir, and on your oath, do you recall ever expressing to anyone any concern that you would lose your license with respect to anything that you did on the National Student Marketing Company audit?

"A No, sir."

You recall that testimony?

A I recall the subject coming up and I just heard you read it, yes, sir.

Q You don't recall it though?

A Verbatim, no, sir.

Q Do you recall that on his cross examination he

also denied having said any such thing to you?

MR. STILLMAN: Your Honor, I do object to this procedure, unless we want to just read all the cross.

THE COURT: All I hear is a question. I don't know quite what you mean by "procedure."

MR. STILLMAN: This idea, your Honor, of confronting one witness with another witness' testimony, my understanding is that is a matter for the jury to determine. I attempted to do the same thing with respect to Mr. Buck and Mr. Velie objected to it at that time. Apparently he now feels it is proper, I object to this.

THE COURT: Since I am not privy to what he is working with, I will ask you, Mr. Velie, what are you working with?

MR. VELIE: Mr. Scansaroli testified and denied certain conversations with Mr. Natelli. We now have Mr. Natelli. I would like to have his version of the matter.

MR. MARTIN: I object to that characterization because Mr. Scansaroli did not deny it.

THE COURT: Whether he did or he didn't is something that we will not decide, gentlemen.

Again, may I suggest that there is an easy way for any examiner to avoid this possible problem raised by Mr. Stillman.

MR. VELIE: All right. We will come back to it, if I may, your Honor.

Q However, this morning you told us a new item of information for this jury, didn't you, about Mr. Scansaroli and this business of losing certificates.

MR. MARTIN: I object, your Honor, to these little speeches.

THE COURT: Yes. I don't think we need that. Let's go back and reframe that.

Q Did Mr. Scansaroli or didn't he say something about losing his certificate to you, sir?

A In a serious vein?

Q Did he ever say it?

A I said this morning what I have some recollection of him saying and that was in a joking vein at one point making a comment such as I have heard perhaps other times from him, perhaps other times -- and other times from other individuals.

Q You tell us what he said at the time you recall.

A I can't recall exactly what was said. It was something on the order of "Hope we don't lose our certificates over this one," or some such thing?

Q He made this little joke, I believe you have testified, just as the two of you were writing off three quarters

of a million dollars of National Student Marketing's 1968 sales, isn't that correct, sir?

A I believe I said that it may have come up at the time that the Ron Michaels problem came up, yes, sir.

Q You say it was a joke.

A That's what I say.

Q Did you pass that little joke on to Mr. Kurek?

A Did I pass it on to Mr. Kurek?

Q Yes.

A No, I don't believe so. I don't think I would have any reason to pass it on to anybody.

Q Mr. Natelli, would you be good enough to tell the ladies and gentlemen of the jury what the term plug means in accountants' slang?

A What the term plug means?

Q Yes, sir.

A The term "plus as would normally be used by accountants would mean to insert as a balancing figure into some calculation or reconciliation an amount that is not otherwise readily identifiable and describable, or has not been identified or described, I guess may be a better way of saying it.

But I would be very careful as to how that word is used because it could have different meanings to different

people in different circumstances, sir.

Q Let's talk about the tax credit that you told us turned up just as the Michaels contracts had to be written off.

A I don't believe -- okay.

Forget it. Go ahead.

Q Just to complete the progress with respect to the questions and answers talking about the certificate, Mr. Natelli, let me go back and read to you some of the questions and answers Mr. Scansaroli answered I believe it was on Friday.

Page 1679.

"Q You told Mr. Natelli you were concerned you would lose your CPA certificate, didn't you?

"A I don't recall making that statement, no, sir.

"Q Do you deny that that's the truth?

"A I don't recall making that statement, sir.

"Q Do you deny that that's so?

"A Do I deny that I ever made that statement?

"Q Yes, sir.

"A I have to deny it, yes, sir."

MR. STILLMAN: Can we go on now? Can you continue with 1681 on that same line?

MR. VELIE: You do that on your time, Mr. Stillman.

MR. STILLMAN: On my time.

Q Do you recall those questions and answers?

A I can't say that I would have before you read them, no, Mr. Velie.

Q You think Mr. Scansaroli forgot about that little joke that you said that he told you?

MR. MARTIN: I object, your Honor, to what Mr. Natelli thinks Mr. Scansaroli would remember or not.

THE COURT: Overruled.

A I don't know if he forgot about that or not.

Q You told us he had made such little jokes several times, is that correct?

A I think he may have I said, yes, sir.

Q Did he or didn't he?

A I can't presently recall other specific instances where he may have, but I believe he may have. It was Joe's nature to be kind of a wisecracker, if you will, at times.

Q We had some testimony from Mr. Scansaroli in which he was read a portion of his SEC transcript in which he said to the SEC that you and he were the only ones who got involved in the tax credit.

Do you recall that?

MR. MARTIN: Objection, your Honor.

THE COURT: Overruled.

Q Do you recall that?

A Do I recall his testifying?

Q Yes.

A I can't honestly say I recall that.

Q Just to set the scene I will read you what I read to Mr. Scansaroli.

MR. STILLMAN: I'm sorry, I do object to this.

Q Scansaroli's SEC transcript, page 222. This is in the record.

MR. STILLMAN: Of course it is in the record.

That's for summation. You are cross examining. Ask him questions.

THE COURT: I don't follow this for somewhat different reasons. I don't understand why we get into this posture.

MR. VELIE: Mr. Scansaroli gave testimony --

THE COURT: No doubt about it. You wish to read him this to refresh him so that you can then ask questions from his knowledge?

MR. VELIE: Exactly.

THE COURT: Fine. I will permit that.

Q Page --

MR. MARTIN: The objection, your Honor, he's not reading from the transcript of this trial, he's reading from the transcript of Mr. Scansaroli's SEC testimony.

THE COURT: However, it is already come out in this trial, correct?

MR. MARTIN: I don't recall the exact contents. That's why I would like to know what was said in this trial.

THE COURT: If you would like Mr. Velie to show it to you, I think you will find that it's already a part of the record in this case.

MR. VELIE: Yes, your Honor.

THE COURT: That's what I think. You want to read

it, Mr. Martin?

MR. MARTIN: I would like to have a transcript reference.

THE COURT: Fine. I would agree with you. You are entitled to that. Just give him a page number, Mr. Velie.

MR. VELIE: It is page 222 of the SEC transcript. It will take a moment to find our trial transcript. We will be happy to do that.

THE COURT: Defense counsel has the SEC transcript. They can follow it from that.

MR. VELIE: Thank you, your Honor.

Q "Q Is there anyone that would have been associated with the job that understood this item?"

And I represent to you, Mr. Natelli, referring to the tax item.

"A Well, I am not so sure anybody would understand unless they went back and reviewed all the figures again. I believe at this time Tony Natelli and I were the only two that really got involved in it.

"Q Did you understand this item?

"A At that time, yes."

Now, Mr. Natelli, were you and Mr. Scansaroli the onlyones who got involved in that tax credit when it came

up and had to be recalculated?

A Are you talking about the time of the tax credit being discovered by -- the tax provision for 8-31-68 being discovered by Carol Raimondo to be in error?

Q I'm talking about the time the Michaels contracts write off was made. Were you and Mr. Scansaroli the only ones who got involved in calculations of that tax credit, sir?

A You have introduced another element. We are talking about a tax calculation that resulted from our tax supervisor, Carol Raimondo, having discovered that in the course of preparing the company's tax return that an error had been made in the prior year in the recording of a provision for taxes, is that correct?

Q My question to you, Mr. Natelli, is a simple one.

Were you and Mr. Scansaroli the only ones involved or not?

A If we are talking about that particular occasion, no.

Q At the time of the Michaels write offs, you say no, you weren't the only ones, is that right?

A You keep introducing another element.

THE COURT: Please, Mr. Natelli. You listen.

Just a moment. You, Mr. Velie, listen to me, too, to make sure I haven't misstated this. Forgetting Mrs. Raimondo for the moment. The question to you is very simple and it could be translated roughly as follows. If I'm wrong about this, Mr. Velie will correct me.

At the time that the original tax deferrment figure was arrived at, did you have anything to do with that or, as Mr. Velie would put it, were you and Scansaroli the only two from PMM who had anything to do with that?

THE WITNESS: I don't mean to be difficult, your Honor. Are you talking -- when you say the original tax deferment, are you talking about the 8-31-68 or May 1969, sir?

THE COURT: You remember Mrs. Raimondo testified about how some time long after the original entry--

A Yes, sir.

THE COURT: Mr. Velie is not asking you about this. This is the reason I'm intervening at this point.

THE WITNESS: That's where I was confused.

THE COURT: All right. That's why I'm intervening, to help you out. You listen, if you don't mind, and we will get it.

Q Let's take it one step at a time.

THE COURT: Go[redacted] back and put it to him step by

step so we make sure he understands here.

MR. VELIE: Thank you, your Honor.

Q When the tax provision, the deferred tax provision was originally arrived at for the purpose of publishing Government's Exhibit 5, the '68 report, did you do that calculation?

A No.

Q Okay.

As far as you know, did Mr. Scansaroli?

A I believe he did, yes.

Q Moving ahead in time, to a point in time in May of 1969, that is the time when the Michaels contracts were written off, isn't it?

A Yes, it is.

Q That time the tax provision was changed, wasn't it?

A It was corrected, yes, sir.

Q Were you and Mr. Scansaroli the only ones who corrected it?

A You mean physically making the entries? I believe that Mr. Scansaroli was involved in making the entries and I believe that I worked with him. I may have worked with him. I'm not sure in calculating what the amount would be.

Q Were you the only ones --

THECOURT: Excuse me. Do you understand the thrust of thequestion here?

Were you and Scansaroli the only two? You say you are not sure about yourself. The question really is: would there have been anybody else besides you two?

THE WITNESS: When you are talking about the entry, your Honor --

THE COURT: I don't want to argue with you, Mr. Natelli: I want to makesure you understand the question.

THE WITNESS: I'm not sure.

THE COURT: You don't know for sure whether or not maybe somebody else on your staff --

THE WITNESS: That's correct.

THE COURT: All right. I just wanted to make sure of that.

Go ahead.

Q Were there, in fact, calculations to correct that tax credit made in or about May of 1969?

A Yes, there were.

Q Were there workpapers with those calculations upon them?

A Yes, there must have been because I believe I recall having reviewed some calculations at that time.

Q Where are they?

A I don't know where they are.

Q If you will simply bear with me a moment, Mr. Natelli.

(Pause.)

Q Do you recall Mr. Scansaroli saying at Page 1687 of Friday's transcript, "I don't think we did any computations, no, sir. There were no computations that had to be made"?

Were there computations or weren't there? What is your best recollection of the matter?

A The sense of computations being to set forth what the correct deferred tax should have been as we understand it as compared to what it had been as recorded, yes, there were some work papers. In fact, I believe -- well, I recall having looked for some of those work papers. I was quite sure they existed. I was never able to find them.

Q I see.

In any event, a tax credit was arrived at and posted into the books at that time in a dollar amount exactly equal to the loss on the Michaels contracts being written off, is that correct?

A Exactly equal to some portion of the Michaels contract being written off, yes, sir.

Q No, exactly equal to those Michaels contracts being written off on that particular entry.

A On that particular entry, yes, sir.

Q The balance of the Michaels contracts were written off later? That was your testimony on Friday, wasn't it?

A Yes, sir.

Q The fact is, Mr. Natelli, there was no tax credit in that amount of 188,750, was there?

A At the time that that calculation was made and those entries were made, Mr. Velie, it was our understanding that there was a tax credit entry necessary to be retroactively adjusted in the 1968 figures.

MR. VELIE: Would you please read Mr. Natelli my question.

(Question read.)

A I will complete my answer then that I have previously given you by saying that it was later determined, in 1970, that that credit was erroneously calculated.

Q That erroneously calculated credit, the error in that was first discovered after the SEC got suspicious and began its inquiries?

MR. STILLMAN: Objection, your Honor.

MR. MARTIN: Objection, your Honor, characterization.

THE COURT: No, I will sustain that as to form only. Rephrase it.

MR. VELIE: Yes, your Honor.

Q Did this error come to light after the SEC began its investigation, Mr. Natelli?

A This error came to light after certain meetings were held, I believe, or phone conversations between the company and certain members of the SEC staff. When you say investigation, I don't believe that it was prior to any formal investigation by the SEC.

Q Let's talk about the Pandick Press for a few minutes.

At the Pandick Press in the early morning hours of August 15, some time after midnight, you finally made yourself clear to Cortes Randall about that Pontiac commitment, is that your testimony?

A I don't believe that is my testimony. I am not sure what you are referring to.

Q Well, you finally made your point that Pontiac would have to be written off, didn't you, right then and there at the printer's?

A I had been making the point that Pontiac based on the documentation that the company had was not acceptable to me for some time, sir.

Q Was your point accepted in the early morning hours at the printer?

A I believe so.

Q Mr.Scansaroli was there, wasn't he?

A At the meeting, yes, sir.

Q You didn't keep this matter a secret from Mr. SCansaroli, did you?

A I didn't have any reason to keep it secret from Mr.Scansaroli.

Q It was an important topic of conversation, a ~~little~~ million ~~middle~~ of the May profit and earnings and sales going right out the window, right?

A As far as the topic being important yes, it was.

Q There was conversations about it throughout the evening?

A I don't know about it throughout the evening aspect. We were doing a lot of work that evening. It was discussed probablymore than one occasion, but it was not a continuous discussion, if that is what you are suggesting.

Q Some time during the early morning hours Mr. Randall piped up and told you about his Eastern Airlines commitment, is that correct?

MR. MARTIN: Objection, your Honor. Can't we just ask questions without having summations? I object to the question.

THE COURT: Overruled.

Q Do you want the question read to you, Mr. Natelli, or do you understand it?

A I would like it read to me, sir, please.

(Question read.)

A I am going to have to try and interpret your question to giveyou an answer.

THE COURT: You say you don't understand that?

THE WITNESS: I am not sure what he means by piped up.

THE COURT: Rephrase it, please, Mr.Velie.

Q Some time during the evening Mr.Randall disclosed to you that he had a commitment from Eastern Airlines, isn't that correct?

A I believe it was some time during that night that Mr. Randall told me that the Eastern Airlines commitment letter was going to be available the next day. I believe that is correct.

Q He said that after he acknowledged that the Pontiac commitment would come out?

A It was probably within the same -- the context of the same conversation.

Q Mr.Scansaroli was still at the Pandick Press?

A I believe so.

Q Still in the same work room with you, if you recall?

A We used the same work room during the entire time we were there, yes, sir. We probably -- it may have been about half the size of this room or a little larger.

Q You didn't keep this matter a secret from Mr. SCansaroli, did you?

A I had no reason to keep it secret from Mr. Scansaroli.

Q When the letter came you discussed it with Mr. Scansaroli, didn't you?

A I don't recall that I did. I don't know if Mr.Scansaroli was there when the letter came. I think he may have departed the meeting before that. I am not positive.

Q Tell us this. One of the things that you had to calculate was whether you would permit them simply to switch Pontiac for Eastern, isn't that correct?

A Yes.

Q YOu did some work, did you, in trying to figure out what the difference is and the money values of these two commitments might be?

A I believe there was some information given to me as to what the expected amount of that Eastern contract

was going to be, yes,sir.

Q That came in over the telephone during the early morning hours?

A I don't believe so, but -- I don't know where it came from. I believe Mr. Kurek had it and it probably came over the telephone, but I think it may have been in the morning hours as opposed to the wee morning hours. I am not positive. It was some time during the stay at the printer's. I would guess it was probably more towards the morning of the 15th, the morning of the work day of the 15th rather than the wee hours, but I am not sure.

Q All of the nine month figures were largely under Mr.Scansaroli's control, weren't they? He was the supervisor in charge of those figures?

A It is somewhat misleading. Certainly Mr. Scansaroli was working on this proxy as was I, and certainly he was working under me and he was in that sense, yes, responsible for the figures that were going into the proxy, if that is what you mean.

Q Does that refresh your recollection as to whether you consulted in any way with Mr.Scansaroli about the Pontiac or the Eastern contracts switch which was being proposed to you?

A I just c-an't honestly say that I recall

discussing it with Joe.

Q There was more than one problem with that Pontiac contract, isn't that right, Mr. Natelli, it wasn't just the wording on the letter?

A I am sorry. I don't know what you are referring to, Mr. Velie.

Q The Pontiac contract, you have taken the position here in your testimony the reason it had to be written off was that the commitment language in the letter wasn't sufficiently strong?

A Yes, sir.

Q Wasn't one of the problems with that Pontiac letter the fact that the company hadn't collected any money at all between February of 1969 and August of 1969? Wasn't that a problem too?

A No, I don't recall that ever being a matter that would have been of my concern, because my concern was with the form of the commitment.

Q This is Natelli's Exhibit H in evidence. It is, is it not -- in fact, it was read to us this morning -- a memorandum of August 7, 1969, between Mr. Kurek and Mr.Randall, and in it Mr. Kurek records conversation which he had the preceding day, on August 6, 1969, is that correct, sir?

A Yes, it is.

Q What Mr. Kurek wrote down was "Yesterday while meeting with you" -- he says with Peat, Marwick, Mitchell & Company. He meant you, didn't he?

A Apparently.

Q "Tony Natelli indicated since we don't have a contract and haven't collected any money on the contract he had reservations about including it in the proxy since it was so near to August 31."

End 3B

He is referring to Pontiac, isn't he?

A Yes, he is.

Q Are you quite sure that one of your concerns wasn't that they hadn't collected a red cent on that Pontiac contract?

A I don't recall it was a concern, because I don't see why that should have been a concern, since I never felt that it should have been recorded in the first place, Mr.Velie.

Q That is your best recollection of the matter?

A My best recollection of the matter.

Q It obviously differs with what Mr. Kurek wrote down the very next day?

A Apparently it does.

Q The Eastern letter was brought to the Pandick Press by Dennis Kelly, wasn't it?

A Yes, it was.

Q That is the same Dennis Kelly who had come up with that Pontiac contract as a post period adjustment to the February numbers?

A I don't recall whether or not I knew at the time that it was also Dennis Kelly, but I believe it is the same Dennis Kelly, to answer your question, yes, sir.

Q It is the same Dennis Kelly?

A Yes, sir. So far as I know, there was only one employed.

Q Do you recall making a note that evening that "To go and replace the GM contract with this" -- you meant the Eastern contract -- "would be really weird"? Do you recall that?

A I wouldn't have recalled it if I didn't have a document to refresh my memory with.

Q It would have been really weird,wouldn't it?

A Excuse me?

Q It wouldhave been really weird, wouldn't it?

A In the context of which that comment was written, that is what I thought at the time,yes, sir.

Q You also wrote yourself a note that says "Wasn't booked" -- you meant Eastern wasn't booked, right --"obviously we are going back and doing something not intended"? Did you write that note?

A It is my handwriting. Obviously that is what I was thinking and that is why I wrote it down for inclusion in the work papers.

THE COURT: Would you tolerate an interruption here for the afternoon recess, Mr.Velie?

MR. VELIE: Of course.

THE COURT: All right. We will take a ten

minute recess, ladies and gentlemen.

(Recess.)

MR. VELIE: May I proceed, your Honor?

BY MR. VELIE:

Q Mr. Natelli, you knew that night at Pandick Press that the emergence of that Eastern contract represented the third time this company had come up with enormous post period adjustments to improve the look of earnings for periods which had already closed, isn't that true?

A I am not sure what three times you are speaking of, Mr.Velie.

Q Let's just tick them off. First of all, I believe you have conceded that 1.7 million of 1968 sales first surfaced two months after 1968 had ended. That is true, isn't it?

A I wouldn't agree that it is true as you have stated it. It is true that it came to our attention as an accounting problem that had to be resolved at that time, yes, sir.

Q And the first records of those 1968 sales all appeared to be dated mid-October?

A The records of those that were placed on the company's accounts as of 8/31/68 -- recorded in their financial statements as of 8/31/68, you are speaking of as

opposed to May 31, 1968, yes, sir, right.

Q The second sentence we have already talked about. The Pontiac contract came up at the end of April to be included in the period which had ended two months before that. That is true, isn't it?

A Which I had never agreed was an appropriate commitment letter. Yes, you are right, yes, sir.

Q You knew that they had done that, didn't you, Mr. Natelli?

A Yes. That was the reason for my concerns that we spoke of this afternoon.

Q Ah, you were concerned because they had done that after the period?

A As to that item,yes, sir.

Q Did it occur to you to be concerned when they did it a third time and came up with this Eastern commitment a full two months after it was supposedly earned?

A Yes, it certainly did concern me.

Q In fact, you might even call that weird too, is that correct?

A You might call what, sir?

Q The fact that they had done this three times, you would call that weird, wouldn't you?

A I don't recall having made any such reference to

that being weird, sir.

Q Would you call it weird?

A I would not call it weird. If you wish to characterize it so, you are permitted to do so, that is up to you, sir.

Q You knew, in short, that this company was juggling its books, didn't you?

A I don't know what you mean by juggling books, sir. That also is a word that can have different meanings by different people who use it.

Q Let's just chew it down for you then. It was not secret to you that the Pontiac contract surfaced just about the time that $1 million of '68 sales were written off? The April 28 letter, you recall, don't you, that the journal vouchers were April journal vouchers writing off $1 million in contracts?

A I must say that I hear what you are saying, but I would not recall -- I did not recall having made the connection ~~with~~ which you are trying to draw, because the $1 million first of all, that you are speaking of pertained for the most part to items that didn't affect the ~~1968~~ 1969 financial statements at all, they affected the 1968 financial statements.

nd 4A

Q No questionthat they came up, both of them, the Pontiac write on and the $1 million write off, in the month of April 1969?

A As matters that came up at that time, yes, that would be true.

Q And there is simply no question at all that you knew that Eastern was being proposed as a flat substitute for the Pontiac contract?

A That is absolutely right, sir.

Q That very night, the night of August 14 and 15 at printers, that was the night that you altered the statements to take out disclosure of the $1 million write off, isn't it?

A No, no, that's not true at all, sir.

Q We are all talking, are we not, Mr. Natelli, about the alterations which appear in Government's Exhibit 17 in your handwriting, right?

A I understand what you are saying, yes, sir.

Q I just want to make sure you know what I am talking about. You say that you didn't do that the night of August 14 and 15 at the printers, is that right?

A No, sir. That's right, that's what I am saying.

Q Let's just have a look then at Government's Exhibit 32 in evidence.

I believe Mr. Schauer identified this as a draft proxy available to him out therein Chicago on August 14, In fact, it bears the date, doesn't it. proof of August 14, 1969.

A Proof of August 14, yes, sir.

Q Let me see if I can rapidly find the footnote for you.

You will agree with me, Mr. Natelli, won't you, that the footnote corresponding to the footnote in Government's Exhibit 17 and Chart no. 10 appears in the August 14 proxy just the way it was before you changed it?

A Yes, sir.

Q I show you Government's Exhibit 19 for identification.

Can you identify that, sir?

A It appears to be a proof dated August 15, 1969.

Q Let's just have a look at the footnote here. The proof of August 15 has the footnote the way it appears in the final proxy, doesn't it?

A Correct, sir.

Q So sometime between the proof of the 14th and the proof of the 15th things got changed, didn't they?

A The proofs got changed sometime between the 14th and the 15th? Yes, I will agree with that statement.

Q Andyou were up there at the printers working away on it, is that correct?

A The evening of the 14th we were up at the printers working on the proxy, that's correct.

Q Part of your work was working on the notes?

A Part of our work was working on notes, yes, sir.

Q Do you still say that you did not do those alterations on the night of the 14th and the early morning of the 15th?

A Yes, I do, sir.

Q Incidentally, the original note is not accurate, is it, with respect to the amount of the adjustment and the amount of the pooled companies line?

A That's right, sir.

Q In fact, it is inaccurate or in error in that it only shows a $70,000 write off instead of a three quarter of a million dollar write off, is that correct?

A That's correct.

Q And the pooled companies are understated by $678,000, is that correct?

A I am not sure of the amount, but it would be the difference between the $70,200 and the total amount of the Ron Michaels contracts that were written off retroactively.

Q That was three quarters of a million dollars,

roughly?

A Some were around that, yes.

Q You knew that this note was inaccurate and in error in that amount when you made your alterations, didn't you?

A I believe I must have known that that amount was incorrect, yes.

Q You must have known because when you did your changes you went and subtracted the 70,000 and the resulting losses from the same place that the first error was made, you went and subtracted them from the pooled companies, too, didn't you?

A Yes. Can we take -- yes, I went to the pooled companies line, and to the extent any of my figures are on the document, it would appear that I made changes to the pooled companies line, if that's what you are asking me, yes, sir.

Q You finished the job then of subtracting National Student Marketing losses from pooled companies instead of from National Student Marketing.

A Finished the job? I am not sure what you mean by that question.

Q Somebody had subtracted --

A That implies that there was an original job that I was fixing, which I don't believe is what I was

doing in that sense of the word, sir.

Q Somebody took $678,000 out of these pooled companies which were National Student Marketing losses, isn't that right?

A That's right. That's what we tried --

Q And he omitted, whoever that was, to take $70,000 of National Student Marketing losses out of the pooled companies, isn't that correct?

A Correct. That's what we tried to explain this morning but you had an objection to, as I recall, Mr. Velie.

Q So you went ahead and polished it off, is that correct?

MR. STILLMAN: Your Honor, object to that.

THE COURT: You mean rounded it off?

MR. STILLMAN: No, no. The polished it off, your Honor.

THE COURT: I am talking to Mr. Velie in answer to your objection.

MR. VELIE: I will change the question.

THE COURT: Rephrase it.

Q You went ahead and subtracted the little remaining $70,200 from the pooled companies, right?

A The effect of the changes that I made were what you have just said because there was a decision that no dis-

closure was necessary, and as I have previously testified, the logical conclusion, having made that determination, was that the adjustment in total should end up on the pooled companies line, yes, sir.

MR. VELIE: Will you please read Mr. Natelli my question.

(Question read.)

Q Isn't that right? Can you answer that yes or no?

MR. MARTIN: I object, your Honor. I think the witness has answered.

THE COURT: Overruled.

A I am not sure if I can answer that question because I am not sure that I inserted that particular figure. But I can't tell from here for sure.

THE COURT: Do you have a copy, Mr. Velie or Mr. Martin?

MR. VELIE: Yes, sure.

THE COURT: It is very hard to read that for Mr. Natelli, I am sure.

MR. VELIE: Here it is.

Q Why don't you take this small copy of the chart and see if you can tell from that what it was that you did? Perhaps the original would be clearer.

A From the original I can tell that the figure in the net earnings portion of that note was changed to a figure which appears in my handwriting.

Q It is exactly $21,000 smaller, isn't it?

A I believe that's correct.

Q So you yourself subtracted the $21,000 of National Student Marketing losses from the pooled companies?

A Yes.

Q Is that why you were telling us that it is probably so that you knew there was an error, because you went ahead and did the balance, subtracted the balance, remaining balance?

A Yes, I believe I testified in looking at this document it appears that I did know where the adjustment ended up at the time because of these notations, yes, sir.

Q It is in error, isn't it? It is improper to subtract National Student Marketing losses from the pooled companies line without any disclosure, isn't it?

A As I testified this morning, it would have been better if I added the words to that line pooled companies reflected it retroactively and other adjustments.

That would have been desirable, yes, sir.

Q You would have to put a note in explaining what the adjustments were, wouldn't you?

A That raises a question as to whether that would need be done or not. There are many instances where such a phrase is used in accounting without any additional disclosure because of the fact that it is immaterial.

Q The fact of the matter is, by the time you were finished with this you had finished subtracting $750,000 of National Student Marketing losses from the pooled companies?

A Yes, I don't believe I have ever denied the fact that the form --

Q Isn't your answer yes?

A Excuse me.

Q Isn't your answer yes? Can't you answer that yes or no?

A If you insist, yes.

Q Fine. There is no disclosure, is there, Mr. Natelli, that that's what you have done?

A No, that's right.

Q In fact, there's no disclosure anywhere in the final note that a million dollars of National Student Marketing losses originally reported had been written off by the time you drafted this note?

A That's correct. I assume youwant me to stick to answering your question exactly. Yes, sir.

Q In fact, when you were all finished the pooled companies reflected retroactively were understated by three quarters of a million dollars, is that correct?

A Yes, sir.

Q National Student Marketing was overstated by the same amount, is that correct?

A Three quarters of a million now, not a million, right.

Q Three quarters of a million?

A Yes, sir.

Q In fact, as you have already said, nobody was ever told that a million dollars was written off?

MR. MARTIN: Objection, asked and answered.

THE COURT: I think we have covered that.

MR. VELIE: Fine.

Q Isn't your best reconstruction of the matter that it was Mr. Scansaroli who did the subtraction of the $678,000 from the pooled companies originally?

A I really can't say that. I don't know if it was Joe Scansaroli or one of the staff working on the engagement. I just don't know.

Q You mentioned Mr. Scansaroli's name in this con-

nection in the grand jury, didn't you? It's been read to the jury.

A In connection with the preparation of the proxy?

Q In connection with subtracting 678,000 from the pooled companies.

A As one of the individuals who possibly may have done it?

Q Right.

A Yes, I did.

Q All right.

A Just as I have here said it may have been him, yes, sir.

Q In fact, the schedule Mr. Martin showed you this very morning, page 2530, Government's Exhibit 13 --

A This is the one we couldn't use this morning, yes, sir.

Q Mr. Scansaroli drafted that, didn't he?

A Yes, sir. It appears to be. It's his initials. I think they are his numbers, all of them.

Q Fine.

I believe you told us the reason you thought it was okay to subtract all of this from the pooled companies, not disclose it, not disclose the million dollars, was that you thought the net amount was immaterial, is that correct?

A That was a major part of the consideration, yes, sir.

Q You were aware of APB No. 9, weren't you?

A Well, I was aware of APB No. 9 being in existence, yes, sir.

Q You were aware that it has to do with disclosure of prior period adjustments?

A Yes.

Q Am I right in saying that APB No. 9 is sometimes referred to as the dirty surplus rule?

MR. MARTIN: Objection.

A Dirty surplus rule? Not to my recollection.

Q Not to your knowledge.

Isn't one of the purposes of APB No. 9 to prevent people from taking this year's accounting problems, dumping them in prior figures and not stating what they had done? Wasn't APB number 9 designed to prevent that very practice, sir?

A I can't really say. I was not involved in drafting that bulletin, but it may be that that was one of the items that it was designed to do, yes, sir. I wouldn't know for sure.

Q You are aware that in paragraph 20 of APB No. 9 -- you were aware of that, weren't you, that even though materia

extraordinary items may net to an immaterial amount, they must be disclosed? Were you aware of that?

A I don't recall reflecting on that in the preparation of this note, but I believe that in general I was aware of it and I think it was done.

Q There was disclosure of the three quarters of a million dollars written off and disclosure of the profit written off and disclosure that you had netted those against a tax credit?

A I believe -- I haven't read that opinion in a long time. I believe the sense of it may be that you don't net either in the financial statement. We did not net them in the financial statement. They are corrections -- corrections were made to the various lines affected by the adjustments.

Q You netted them in the privacy of your accounting office or at least at the Pandick Press, isn't that correct?

MR. MARTIN: I object to that, your Honor.

THE COURT: No, I will allow that.

A I'm not following you now. I just answered a question. I don't understand the question you asked.

THE COURT: We will have it rephrased.

Q There is no disclosure, is there, Mr. Natelli, of the fact that you went and offset this tax credit against

the profits written off on the Michaels contracts? That's nowhere disclosed in that proxy, is it?

A When you say disclosure, and you refer, I presume, to narrative statements, obviously I have explained here why there is no narrative explanation. As to the figures being where they belong in the statements, they are appropriately adjusted to reflect the changes that we thought had to be made, sir.

Q There's no adjustment whatever, is there, to the number originally reported for National Student Marketings net sales for 1968?

It is still approximately five million bucks despite the fact that a million had been written off?

A I don't believe that -- I don't know what your question is, but I don't believe that that accounting principles board opinion was in any way, shape or form designed to apply to a footnote of that nature.

Q That is your explanation?

A That's what I believe my explanation is. I believe that opinion applies to the financial statement itself, a statement of earnings. At least the portion where you are talking about it's not being netted, that is either being placed where they belong, in the broad sense. That means they should be so placed in the financial statements. That's what

we did.

Q That's your explanation?

A Yes, sir.

MR. STILLMAN: It's sworn testimony.

Q Would you please show me where there's any explanation at all for the reader to know that a million bucks got written off at all, where the numbers have been changed, a million dollars going right out the window? How can anybody find that in your proxy?

A They can read the statement of earnings, and when they read the statement of earnings, it has already been corrected for these adjustments.

Q Secretly?

A Secretly?

Q Nobody can tell what's happened to those numbers, isn't that correct? Isn't it the purpose of this note to reconcile what was originally reported to what you have put in the earnings statement?

A The purpose of that note I believe is to give the trend of net earnings of the company as it now exists as of a prior date in time, that is the elements that would be placed in the company's prior reported figures with the elements that were in the prior company's reported figures as of the preceding report as to revenues and net earnings; just those two lines yes, sir.

Q Take a look at Note D.

Does it not say that net sales and earnings as originally reported for certain years are reconciled with the earnings in the proxy? In other words, this is an explanation or reconciliationfrom what people originally read in that big statement of earnings as pooled together in your proxy?

A Yes, as to the two elements, that's right.

Q You don't dispute the fact that APB No. 9 requires that whenever prior period adjustments are made, they must be disclosed? Did you dispute that?

A That is difficult to see,what you are reading out of context. I would not dispute that that statement is made in there.

THE COURT: Would you like to see this material he is reading from?

Q I amgoing to read to you a portion of this right now.

"The board further recommends that whenever prior period adjustments have been reported during any of the periods included therein, the reported amounts of net income and the components thereof as well as other affected items be appropriately restated with disclosure."

That is what it says, doesn't it?

A Yes. That portion of it reads as you say, yes, sir.

Q Now, sir, had you forgotten that this portion existed when you did this work on this particular proxy note?

A I can't say that I focused on that portion. It is obvious when I first drafted a note, when I had intended that these -- let me change that -- when I had determined that these adjustments should be made retroactively, that I felt disclosure was appropriate. By the time -- as I have explained in my testimony, by the time I got looking at my note, again in another draft, and made the various considerations, gave the various considerations as I indicated in my testimony, I decided that it was no longer necessary to give that disclosure and I explained the reasons why. I believe that you will find that in any of these accounting principles board opinions, there is usually some reference to materiality being the matter of the judgment in any instance.

Q You don't ordinarily restate a prior year for material amounts, do you?

A No, that's correct.

Q Okay. You did restate a prior year here, did you?

A Yes, we did.

Q This is the sales portion of the footnote in the proxy, is that correct?

A Yes.

Q All right. You have told us that $748,000 got subtracted from the pooled companies.

Do I have you right, sir, in saying that was an error?

A An error?

Q It shouldn't have been subtracted in that fashion without any disclosure, should it? Is that a mistake?

A I wouldn't call it a mistake so much as I would call it an adjustment that was made as to how these amounts should be adjusted.

Q Didn't you think that it was an error when you testified in the grand jury, characterized it as an error there?

A I believe if you wish to read what I said in the grand jury, so it would be fair in what I am trying to recollect, I would be glad to have you do it, sir.

Q I am reading from Page 45 of the November 23rd --

MR. MARTIN: November?

MR. VELIE: November 23.

Q "Now, when you received the proof, did you recognize that an error had been made?

"A I honestly do not know. I would say I probably did. I cannot recall my attention was directed at the disclosure of this item and what had to be said to, if anything, disclose it.

"Q Do you remember calling the error to anybody's attention?

"A I can't recall exactly, but I must have."

You go on to explain from there.

You didn't disagree then in the grand jury that this was an error, did you?

A The error being spoken of there is the $70,200, that is correct.

Q No, $678,000.

MR. MARTIN: Can we fix what proof he was being asked about in the grand jury?

MR. VELIE: What is now Government Exhibit 17. This portion you will recall was read into evidence from the Government's direct case, from Pages 41 to 47, and the exhibit shown to Mr. Natelli was identified at that time as being Government Exhibit 17, the draft with his own handwriting on it, Mr. Martin.

Q Do you want me to read you enough so you will

see --

A My recollection of the context of that comment was that it was pertaining to the question of the net pooled company line as you previously discussed here, having had included in it a portion of the adjustment that belonged up on the line for retroactive adjustments.

Q The $678,000, is that correct?

A Should have been up $70,200.

Q Putting it in the pooled company's line, you characterized or agreed at the time you were in the grand jury it was an error?

A That is where you are twisting it a bit, sir. The error was in that particular presentation where it was intended that there be a million dollar line that had the retroactive adjustments disclosed in it. The amount included on that line was an error because a portion of it was down below. I believe that is the context of that testimony, as best I recall it.

Q Let me just see if I have it correctly then. It was your intention then and it was not an error that $75-,000 come out of the pooled company's line without disclosure? Which was it? Was it an error --

A You asked me about my grand jury testimony --

Q I am asking you to take a look at this number

which says pooled companies reflected retroactively.

MR. MARTIN: Objection, your Honor.

Q It is, as you have already conceded, understated by three-quarters of a million dollars resulting from the fact that three-quarters of a million dollars was National Student Marketing's losses and it was subtracted from the pooled companies. Now, I ask you, did you intend for that to happen or was it some kind of an error?

MR. MARTIN: I object to that, your Honor. It is two different periods of time to go in one question.

THE COURT: No, I don't think so. I think now we are dealing with what his intention was, what his understanding was at the time when this proxy material, those figures, so on, were being prepared and the footnotes were being prepared.

A At the time that that footnote ended up in the final form, if that is what you are asking me, I did not believe we had an error in the presentation in that it was an adjustment where disclosure was not necessary in narrative form of these items, and, consequently, as I explained in my testimony, that would have been the logical place where this amount would come to rest since it is between the originally reported and the then current reported statement of earnings. It is the one line of adjustments.

Q There is no question that these pooled companies were acquired after the year ended 1968?

A Yes, that is correct.

Q They didn't lose this money?

A They didn't lose the money? No, that is correct.

Q You subtracted it from there?

5B A That is correct.

Q This is the earnings portion of the line. The fact is that roughly $210,000 was the gross profit on all the Michaels contracts which were written off, isn't that correct?

A That's correct.

Q That is not disclosed in here, is it?

A No, it is not.

Q You offset that $210,000 item with an unrelated tax credit in the amount of $188,000, isn't that correct?

A We offset it? That is the logical result of accounting in this case, that you would have a gross profit and then you would have a tax adjustment. Yes, that is a correct statement.

Q This tax adjustment is not an adjustment to this figure, is it, it is a tax adjustment to the deferred tax account for the entire year 1968 and not specifically related to these contracts?

A Well, as it turns out a portion of it is related to these contracts, yes.

Q But not the whole thing, is it?

A No, that's right.

Q And yet you netted these unrelated items, isn't that correct?

A You have to net them to get to the net earnings

line, sir, yes. That note has to do with net earnings and the effect on that earnings is $21,000.

Q None of these three things were disclosed, they were simply quietlydone by you and the final result swallowed up in the wrong line, is that correct?

MR.MARTIN: Objection, your Honor, argumentative.

THE COURT: I am wondering whether you yourself want to put swallowed up in one line.

MR. VELIE: Very well.

THE COURT: Rephrase it.

Q You did not, did you, disclose the components of the retroactive adjustment you had made or retroactive adjustments you had made, did you?

A That is correct, we did not give any narrative disclosure to it, yes, sir.

Q And one of the components was the total of the three Michaels contracts written off plus the fourth, $210,000 profit written off?

A Yes.

Q There was a largely unrelated tax credit also not disclosed separately, is that correct?

A That's right, largely unrelated.

Q And the difference was $21,000 of writeoff

earnings, is that correct?

A Yes, that's right. That is a result of the two unrelated items that were separately discovered, yes, sir

Q You personally subtracted this particular National Student Marketing loss from pooled companies which didn't lose it, isn't that correct, sir?

A Yes, it is.

Q Is that a mistake or did you intend to do that?

A I am quite sure that when we were finished with that draft we intended to do that, I intended to do that.

Q Just so there is no mistake about it, when I was talking to you about that tax credit earlier, this credit here in the amount of $188,750, after the SEC inquired it turned out there wasn't any tax credit in that amount, was there?

A It was, as I previously explained, determined after an inquiry by the SEC that that $188,000 was incorrectly calculated, yes, sir.

Q When you spoke of Mr. Otkiss, he had before him, did he not, if he did have anything before him, the footnote -- whatever he had before him was the footnote in its first version, isn't that correct, the footnote which discloses only $70,000 as a writeoff? Do I have that right?

A Yes.

Q You didn't tell Mr. Otkiss, did you, that $678,000 of National Student Marketing losses had been subtracted from the pooled companies, did you?

A I don't recall the detail of the discussion, as to where any adjustments might have gone in that note. However, I do know that we discussed the total circumstances of the Ron Michaels writeoff as well as the taxes. Consequently, in view of the amounts that we were dealing with that netted to $21,000, we must have discussed the overall amounts in question.

Q Please, Mr. Natelli, did you or didn't you tell Mr. Otkiss that $678,000 of National Student Marketing losses were subtracted from the pooled companies --

A I didn't know.

Q -- which didn't lose them?

A I don't know.

Q Ah, you don't know.

MR. STILLMAN: Your Honor -- all right. If he wants to perform we will watch him perform.

MR. VELIE: Can we have that remark stricken, please.

THE COURT: It will be stricken.

Q Did you tell Mr. Otkiss that you proposed to

subtract yet another $70,000 of National Student Marketing losses from the pooled companies instead of from National Student Marketing? Did you tell him that that is what you planned to do?

A I don't recall whether I told him about the detail that you are bringing up here as to an error in a proof that had to be corrected. I don't know.

Q Mr. Otkiss was interested in the way the company had reported on percentage of completion accounting, isn't that correct?

A Yes.

Q Did you tell him at any time that $3.3 million of unbilled accounts receivables booked over the 18-month period starting when contracts were booked for '68 and going through the first six months of 1969 -- did you tel him that two million of those $3.3 million had been written off?

A I can't recall telling him in the phraseology that you just used as to what happened. If you wish me to tell you what I can recall telling him I would be pleased to do so.

Q Let's put it this way. Mr. Otkiss said that you were speaking about one particular situation involving five, six or seven thousand dollars. Is that what you

told him?

A With respect to Ron Michaels? Yes, sir.

Q With respect to the performance of the company on unbilled accounts receivables, is that what you told him?

A At what time now? When we were discussing this draft note regarding Ron Michaels or when he first talked to me on the telephone about the overall method of accounting?

Q Did you ever bring to his attention when he was trying to figure out whether this was a good method of accounting or not -- did you ever bring to his attention the fact that two out of $3.3 million of sales had been written off, at any time?

A Once again, I can't answer the question in the specifics of the terminology that you are using. If you would like me to explain what I recall telling him I would be glad to.

Q Mr. Natelli, did you point out to him that of t '68 sales alone $1 million of $1.7 million had already been written off?

A Effectively, I believe I did, because I explained to him about the Ron Michaels contracts and I did tell him that there were certain other items that the company had written off during the I guess it was the first six months of '69.

Q So it is your testimony that you did tell him a million bucks had been written off?

A Once again, you are putting words in my mouth that I don't wish to be there. I don't recall if I used the $1 million. $1 million was not a term that I focused on until hearing it from you so much in this courtroom.

I did tell him about the Ron Michaels contracts and I did tell him about certain other contracts the company had written off, the amount of which I don't know if I had specific number on at the time.

Q Did you point out for Mr. Otkiss your view that the contracts would make or break the company?

A I don't recall having said any such thing to Mr. Otkiss, no.

Q Did you point out to him that you thought that all 3.3 million of these things were uncollectible?

A Did I point that out to him?

Q Yes, sir.

A I never believed it, so how could I point it out to him.

Q I have reference to Government's Exhibit 16 and to something I read to you earlier today. "It is important that $3.3 million is unbilled in the balance sheet. Suppose we do run into problems. Will you sue them? Doubt if you

have a case. I've got to look at the negative."

My question to you, Mr. Natelli, is did you ever say anything like this to Mr. Otkiss?

A At the time we were discussing this note I don't recall having discussed it with him, no.

Q Did you point out to Mr. Otkiss that the company had three different times pumped its earnings with after the period additions of enormous unbilled accounts receivable?

A Three different times?

Q We went through this. $1.7 million in '68, Pontiac after the period of the six months, Eastern.

A Let me—

Q Did you tell him about that?

A In substance, yes, because Mr. Otkiss was aware of what had transpired in '68 in terms of responding to his questions about the accounting, he was aware of the fact that the Pontiac contract is something that I did not agree with, and he in fact concurred with me on the Pontiac letter, and subsequently I discussed with Mr. Otkiss the Eastern contract, which I decided should be permitted by the company to be booked. So if those are the items you are talking about, yes.

Q Did you tell him that the Eastern letter came up at 3 o'clock in the morning just as you were writing off

the Pontiac? Did you point that out for him?

A I discussed with Mr. Otkiss the fact that the Eastern letter was given to me at the printer and I discussed with him what the contents of that letter were and why I considered that it was permissible for it to be booked and I recall him agreeing with me.

Q I asked did you point out that it came up exactly as Pontiac was being written off, about 3 o'clock in the morning at the printers.

A I don't recall that it came up exactly at 3 o'clock in the morning at the printers when Pontiac was being written off, as you suggest.

Q Is that your testimony?

A Yes.

Q Do you recall Mr. Otkiss appearing here and testifying, at page 1767?

"We had a discussion of the Pontiac contract. As I understand it, at the time it was not a matter of something that was written off, it was a mater of something that was not a written commitment at the time. Mr. Natelli informed me that he would not permit them to book that type of contract."

I ask you, sir, is that what you told Mr. Otkiss?

A I am quite sure that Mr. Otkiss at the time was

aware that the figures in the proxy had the Pontiac commitment in it?

Q That's not what I asked you. I asked you if that's what you told Mr. Otkiss.

A No.

Q What did you tell him? Did you tell him that in fact it had been earnings of the period ended six months, the February figures? Did you tell him that?

A I don't recall that.

Q And that in fact it was a $1 million write off not disclosed to the shareholders or the public?

A I recall that it was in the figures as contained in the draft of the proxy, which were the May figures, and consequently something the company had already booked. I don't recall whether we discussed whether or not they were in the six months figures.

Q Let me just see if I understand you.

A I am not sure.

Q Mr. Otkiss when he testified here was wrong when he said that he didn't understand that it hadn't been booked, you are saying that you told him it had been booked and had to be written off and when he came in here and testified he was in error, is that correct?

A I really don't know. I don't know whether you

got into the detail that you are getting into with me when you chatted with Mr. Otkiss. I don't remember. I can't tell you whether his testimony as he thinks he testified is correct or not. I am telling you what I recall about the situation.

Q All right, Mr. Natelli. Mr. Scansaroli told you about the Oberlander schedule, the August schedule, didn't he?

THE COURT: Excuse me.

If I sense correctly that you are going to another subject, may I suggest we suspend now for the evening.

MR. VELIE: I am.

THE COURT: All right.

Mr. Lights and ladies and gentlemen, we will adjourn until tomorrow morning at the usual time, 10 o'clock. Have a good evening.

(Jury left the courtroom.)

MR. STILLMAN: Judge Tyler, I wonder at what point your Honor would have time to enlighten us on your rulings on the requests, so that we might be able to --

THE COURT: I would like to wait until I hear the evidence complete, which I think is only a fair request on my part.

MR. STILLMAN: I appreciate that. I am just

really trying to factor in how to handle what it is your Honor is going to tell the jury in my summation.

THE COURT: You will rest assured that, as the law requires, you will hear from me before you sum up.

MR. STILLMAN: Fair enough, your Honor.

THE COURT: But I insist that it is reasonable for the Judge on his part to ask that the case be over before he make any such splendid rulings.

MR. STILLMAN: I rarely suggest that judges are unreasonable. Thank you.

THE COURT: You see my point?

MR. STILLMAN: Yes, I do.

THE COURT: I assume from what you gentlemen tell me that hopefully this will come up sometime tomorrow morning?

MR. STILLMAN: Yes, sir.

THE COURT: All right.

(Adjourned to 10 a.m. November 12, 1974.)

UNITED STATES OF AMERICA

-vs- 74 Cr. 43

ANTHONY M. NATELLI
JOSEPH SCANSAROLI,

November 12, 1974
10:00 a.m.

(Trial resumed, in open court. Jury present.)

xx A N T H O N Y M. N A T E L L I, resumed.

THE COURT: Good morning, ladies and gentlemen.

Mr. Velie.

MR. VELIE: Thank you, your Honor.

xx CROSS EXAMINATION (Continued

BY MR. VELIE:

Q Mr. Natelli, Mr. Scansaroli told you about the existence of the Oberlander schedule, didn't he?

A Yes, I knew about the Oberlander schedules, that is, the Oberlander questions on certain fixed fee items.

Q You knew that he had found many items to be questionable, is that correct?

A I knew Mr. Oberlander had requested certain items, yes.

Q You knew that he found many items to be bad, is that correct, sir?

A I knew he had questioned certain items to be bad, yes, sir.

Q Did you actually look at Mr. Oberlander's schedule?

A No, I did not.

Q You were the partner in charge of the SEC review at that time, is that correct?

A Yes, I was.

Q You did not look at the schedule?

A That's correct.

Q Did Mr. Scansaroli tell you what the items were on the schedule and what they amounted to?

A I had some knowledge of what the amounts were that were being discussed. I did not ask Mr. Scansaroli for any of the details and consequently I don't recall that he told me any specific items.

Q Did Mr. Scansaroli tell you that virtually all of these items had been sitting there on the books since August 31, 1968?

A I can't say at this moment for sure that I knew that they were all '68 or not, but there may have been some discussion of that.

Q Did Mr. Scansaroli tell you that in his own review several months before, in May, he had found six of them himself in large amounts to have been highly suspicious and not

at all good sales?

MR. STILLMAN: Object to the characterization, your Honor.

Q Did he tell you about what he had found with respect to these six sales?

A I can't recall any discussion of any correlation of items that were --

Q Did you do any investigating at all to find out whether in fact some $300,000 worth of commitments, gross numbers, were simply no good?

A Yes. I asked Mr. Scansaroli to follow up on Doug Oberlander's questions and he reviewed them.

Q But you didn't look at the schedule?

A No, I didn't, no.

Q And you didn't determine that they had been sitting there since '68?

A I didn't personally, no.

Q And you didn't determine that they had been questioned before?

A I did not.

Q Ycu agree, do you not, Mr. Natelli, that this chart summarizes the contracts which were still on the books as of the May period which is shown in the proxy statement, is that correct? These contracts had not been written off,

they were sitting there on the books as of the May figures, is that correct, sir?

A Based on testimony that has been here, considerable discussion about that schedule, I believe that it has been indicated that these are some of the specific items that were on the schedule. I don't have a familiarity with the schedule in any detail that I could make such a conclusion myself at this point, if that's what you are asking me.

Q You are not disputing it though, is that the idea?

A I have no reason to dispute it, based on whatever testimony there was.

Q You don't dispute the fact that the work papers show entries such as are summarized here, Mr. Scansaroli's review in May, Mr. Oberlander's review in August, do you?

A I have no reason to. If I had some familiarity with the work paper, I may or may not dispute the particulars of what you have there. But I have no reason to since I have no familiarity with the work papers.

Q There was no disclosure of any of the matters summarized on that chart, that is, the comments and the questions here, no disclosure of that bad news in the proxy statement, was there?

A Was there disclosure of these detail amounts? No, sir.

Q Was there disclosure of the fact that Peat, Marwick accountants had on two occasions questioned contracts of this kind in this amount, any warning to the readers of the proxy statement that the Peat, Marwick accountants, including Mr. Scansaroli, had these questions?

A No, there wasn't. That doesn't imply, of course, in my answer that there was any consideration that there should have been.

Q In fact, you don't dispute the fact that Government's Exhibit 25, the proxy statement, in the description of the business of National Student Marketing, on page 16, describes the business of the company, order of profitability, and lists at the top fixed fee contracts, the most profitable item this company says it has.

MR. STILLMAN: Your Honor, the document is in evidence. It speaks for itself.

Q Do you dispute that?

MR. MARTIN: Objection, your Honor.

THE COURT: I will allow that.

A If that's what it says, I don't dispute it.

Q Were you aware of the fact that the company was telling the public that this was its most profitable way of doing business?

A I can't honestly say that I recall focusing on

those items that are in the so-called forepart. I must have read the document at the time, during its preparation, but I don't recall focusing on it at this point.

Q Let's talk about the comfort letter for a minute. Just so we are clear, you will recall Mr. Frommer's testimony -- just so you know who we are talking about, Mr. Natelli, he is the gentleman who testified that he sold the company he calls Europe on $5 a day, or whatever the travel company is called. He sold it for National Student Marketing stock. You remember him?

A Yes, I remember the individual.

Q He closed his deal sometime in the middle of October. That's right, isn't it? You recall that testimony?

A I can't honestly say I recall that testimony, but I won't dispute that if that's what the facts are.

Q You never sent him the information contained in that comfort letter, didyou, at any point?

A I can't recall whether I did or didn't. I didn't send the comfort letter information to anyone outside of NSM. I don't know if he was a recipient of the comfort letter, if that's what you are asking me.

Q You didn't see to it, did you, that Mr. Frommer learned what it was that youlearned about the comfort letter adjustments, did you? Did you make it your business to do

that?

A I can't recall whether that was one of the companies that I indicated to Mr. Kurek he should make sure that he disclosed the comfort letter contents to. I just don't recall.

Q As I recall it, you did that for the later acquisitions, Cottrell, Ritzenthaler, Stuckey & Speer.

A Well, I believe, to be clear on that point, I believe that what I told Mr. Kurek that in my opinion I felt that he should do is to make sure that any acquisition companies that the company was merging with, which companies may have relied on information in the proxy which we then knew on the basis of the comfort letter review was in error, that he should see to it as part of his responsibility that those companies were informed about the comfort letter contents.

Now, I honestly don't recall reflecting on any particular company at the time, as to whether it was or wasn't one that should have been included in that general context of what I told Mr. Kurek.

Tk 1B

Q Mr. Natelli, you didn't see to it that the companies that had already been acquired learned that information, did you? Not the ones that they were about to acquire, but the ones which they had already acquired.

A Well, I would have to just refer to my previous answer as to what I recall, to the extent I recall telling Mr. Kurek what I thought he should do.

Now, if inthat general recommendation to Mr. Kurek something would have fallen through the crack, as you are just suggesting, I don't know. I just don't know the answer to that.

Q Let me ask you something else about that comfort letter. When Mr. Colona spoke to you on October 31 he had already reached a definite conclusion about those particular adjustments, hadn't he, he had decided that they had to be disclosed as written off as of the May period?

A Yes, he and Johnny had come to that conclusion, and that is why he was calling me , right.

Q You didn't add anything further to that comfort letter, did you?

A I didn't have anything that I thought should be added, so I didn't add anything, that is correct.

Q You knew there had been another $1 million written off during the period and not disclosed anywhere?

A Well, once again, the $1 million is your figure.

Q It is the Pontiac contracts.

A The $1 million is the Pontiac?

Q Yes, written off during the May period and not disclosed anywhere, was it?

A Well, by your definition it is something then that would not have been a matter of a comfort letter, sir.

Q Oh? Isn't it a matter of interest to a person who wants to buy the stock of the company that during the very period that you are reporting a $1 million contract got written off because it was worthless, another contract got substituted in, and nobody got told about it?

A Now you are jumping from a comfort letter to interest of somebody who is buying stock inthe company. That comfort letter had a very specific purpose related to a specific closing with a merger company. It had certain guidelines as to what was to be included in it. It was based on information that we were to obtain based on review of the company's records after May 31, 1969, up to the date of the closing, and the comfort letter consequently included what we considered based on that review to be includable.

Q The comfort letter, Mr. Natelli, was addressed, was it not, to the Interstate people, who were in fact about

to buy National Student Marketing shares, they were going to give up their shares in their company and buy National Student Marketing shares, is that correct?

A The comfort letter was addressed to Interstate and National Student Marketing, both,as I recall,and it was pertaining to the closing in which Interstate shareholders would be exchanging their shares for National Student Marketing shares, yes, sir.

Q Is that your answer?

A That's my answer.

Q All right. Now, you knew, didn't you, that Peat, Marwick's lawyer and Peat Marwick's professional practices committee were trying to figure out whether they had to tell the SEC something about National Student Marketing over the weekend which began on October 31, you were certainly aware of that, weren't you?

A Oh, yes.

Q There was an itemof testimony here, that Mr. Kurek, as I recall it -- perhaps you recall it differently -- said something to the effect that he overheard you say something on the telephone to either Mr.Davies or Mr.Joy in which he thought you might have recommended that they go to the SEC.

I want to ask you, Mr. Natelli. Did you tell

Mr.Davies or Mr. Joy that they should go to theSEC?

MR. MARTIN: Objection, your Honor. The testimony was that it was said in a conversation with Mr. Epley.

Q All right, Mr. Epley. Is that what you told him?

A Yes. My recollection is that in the course of one of the conversations that day, in discussing the fact that the comfort letter was not yet finalized and that we had also not considered what else might be something that we should recommend might be done, that one of the items that we had under consideration was whether the company should go to theSEC, yes, sir.

Q That is what you said, wasn't it, one of the items that you had under consideration was maybe going to the SEC? That is just what you told us, that is your testimony, isn't it?

A Whatever my testimony is. It is clearly the point that we had under consideration the fact that one of the items that the company should do perhaps is go to the SEC, that's right.

Q Thank you. Now, while all these matters were under consideration by Peat, Marwick's lawyer and under consideration by Peat, Marwick's professional committee, professional practices committee, you had a talk with Mr.

Scansaroli about the comfort letter adjustments, didn't you?

A I believe that some time after the issuance of the comfort letter I had a discussion with Mr.Scansaroli. At least, that is my best recollection at this time.

Q I am going to show you Mr. Holton's memorandum. I have marked it as Government Exhibit 67 for identification. I believe it also has a defense number. It is Mr. Holton's memorandum I believe you will see of November 5, 1969, identified by Mr. Holton here and used by him to refresh his recollection.

Just take a look at this line here, "I discussed this matter in the morning," and read through where it says "In the meantime Mr.Natelli had discussed," and so on, and see if that refreshes your recollection, sir, as to whether while the matter was under consideration you had a talk with Mr.Scansaroli.

MR. VELIE: For the record, apparently I used Government Exhibit 67, as I recall it, to refresh Mr. Holton's recollection. It did not have a defense number.

Q Have you read some of that, Mr. Natelli, to refresh your recollection as to when you talked with Mr. Scansaroli?

A Yes. I can't say that it helps a great deal, but --

Q YOu have refreshed your recollection?

A Yes.

Q With your recollection now refreshed, can you tell us, did youtalk with Mr.SCansaroliwhile the matter was under consideration of going to theSEC?

A No, I can't say that that helps me identify whether I spoke to him while it was being considered, whether I should go to the SEC. It must have been before M. Holton drafted that memo, which has a date of November 5, which is what, we said today?

Q In any event --

A It was before the date of that memorandum, which I belive is a Wednesday. My best recollection is that I discussed it with Mr. Scansaroli after the comfort letter problems, after we had decided what to do with it and in connection with that Mr. Holton and I had discussed as to whether there was anything that happened with respect to this comfort letter and the problems we discovered.

Q There is no question before you except did you talk to Mr. Scansaroli? You can answer that yes or no, can't you?

A Did I speak to him?, I told you I spoke to him.

Q Let me ask you another question,sir. Did you also speak with Mr.Joy? You can answer that yes or no.

A Yes, I believe I spoke with Mr.Joy.

Q After you talked with Mr.Joy and after you talked with Mr.Scansaroli, you reported to your superiors at Peat,Marwick, Mitchell & Company that you thought that the company had just made an honest mistake with respect to those comfort letter adjustments, didn't you?

A Yes, that's right. Absolutely.

MR. VELIE: Thank you.

REDIRECT EXAMINATION

BY MR. MARTIN:

Q Mr. Natelli, do you recall being asked by Mr. Velie about the work that was done by Mr. Sullivan? Do you recall that area of cross-examination?

A Yes, I do.

Q Do you recall also, Mr. Natelli -- I put before you what is now Government Exhibit 46A in evidence and ask you, sir, did you have occasion to see that document in September or October of 1968?

A Yes, my recollection is that I did.

Q What is that document, sir?

A This document is the financial report issued by NSMC to its shareholders for the nine months ended May 31, 1968.

Q What does that document report as the profit of NSMC for that nine month period?

A $288,000.

Q Did you have occasion to discuss the preparation of that document with anyone or the compilation of the figures that went into that document?

A No, noti n any detail.

THE COURT: Do we understand you correctly as to the dates? You say for the nine months ending May 31, 1968.

THE WITNESS: Yes, sir.

THE COURT: Your people wouldn't have had anything to do with preparing that, would they?

THE WITNESS: No, in preparing it, not at all.

THE COURT: Not at all.

THE WITNESS: That is not the question that counsel asked me.

THE COURT: That is what I am trying to get at.

As I see it, based on whatyou have already told us, youwouldn't have discussed this with anybody?

THE WITNESS: The preparation of the nine months figures?

THE COURT: Yes.

THE WITNESS: That is correct.

THE COURT: I don't follow the relevance of this.

MR.MARTIN: Let me try another question, your

Honor.'

Q Did you learn inSeptember or October of 1968 of who prepared that document?

A Yes, Mr.Kurek told us that he and Mr. Sullivan worked together in preparing it.

Q Did you learn in the fall of '68 whether or not income had been recognized at the time commitments were obtained in the preparation of that document?

MR. VELIE: Excuse me.

A Yes, sir.

MR. VELIE: I object to putting words in the witness' mouth. That is a leading question, your Honor, that is not necessary.

THE COURT: It may have been leading. I couldn't understand it. I couldn't hear it. Since we are in that posture, why don't you just rephrase it, Mr. Martin.

Q Would you tell the ladies and gentlemen of the jury, did you have any conversations with Mr. Kurek about this?

A Yes, I believe I previously testified that in the course of discussing what accounting method would be appropriate for the fixed fee type business, we were advised by Mr. Randall and/or Mr. Kurek in his presence at least that this method was used when Mr. Kurek and Mr.

Sullivan prepared the nine months figures to the shareholders, May 31, 1968.

Q Did you have any reason in the fall of 1968 to believe that Mr. Kurek was lying to you, sir?

MR. VELIE: I object to any suggest that Mr. Kurek lied to anybody. That is a completely false question.

THE COURT: Before we even get to that, I don't follow this from another point of view. It seems to me we are getting into a totally new area here.

Second of all, this question seems to me to be unconnected with anything in the record so far.

I am sorry, Mr. Martin, but for those reasons --

MR. MARTIN: Your Honor, I think there was questioning as to what he did as to checking on --

THE COURT: That is something else again, Mr. Martin. Now we are getting into a question as to whether or not this witness in his opinion ~~through~~ thought that Kurek was lying, which I think is quite a different animal.

If you want to put something about checking, I agre with you, that is relevant.

Q You were asked on your cross-examination about a conversation and you were given a memorandum which I believe is the September 19, 1968 memorandum.

(Pause.)

MR. VELIE: Is that the memo to Phillips?

MR. MARTIN: Yes.

MR. VELIE: '59.

Q And you were asked some conversations that you had with Mr. Joy in September of 1968.

Do you recall being questioned about that?

A Yes, I do.

Q What was Mr.Joy's position at the time you talked to him in September of '68?

A He was a partnerin the investment banking firm of Hutton & Company and a member of the board, I believe. I am not positive at that point whether he was. I think he was a member of the board of National Student Marketing Corporation, but his occupation was partner in the investment banking firm.

Q What was Hutton & Company?

A An investment banking firm.

Q Have you overnight had an opportunity to review that document?

A Yes, I have, sir.

Q Will you tell us now what you recall was the discussion that you had with Mr.Joy, what you said and what he said, as best you can recall? First tell us now, though, sir, was this in person or by telephone?

A I am quite sure it was during one of the telephone conversations I would have been having with Mr.Joy at this time.

End 2A

Q Would you tell the members of the jury what the substance of that conversation was as best you can recall, what you said to him and what he said to you?

A As best I can recall, it was a discussion that I had with Mr. Joy pertaining to what I understood was a proposal that NSM was considering to split its shares or recommend to the stockholders that the shares be split at the upcoming annual stockholders meeting.

As a result or since there was a high multiple in the company shares, I think that I had raised a question with him -- this may have come from a discussion with Mr. Phillips in the New York office -- raised the question to him as to whether or not there was any problem here since there might be some additional increase multiple from the split. It was that kind of a conversation.

In the course of discussing the question of high multiple of shares to me, which is of course, what Mr. Joy's interest was, being an investment banker, not an accountant, he explained to me that they had given consideration to the factor that I had raised and, in fact, they didn't think that would be a problem or would occur from his standpoint.

I didn't really have an interest in that.

He also said that the reason for the split had only to do with their desire to have an increased amount of shares looking forward to eventual listing on one of the exchanges,

which is one of the things that would have been necessary.

It was in the context of this that Mr. Joy indicated to me that they -- that is the investment banking firm of Hutton and Company -- was constantly reviewing the background of the transactions in NSM shares to make sure that whatever the multiple was, that it wasn't caused by any -- these were his words -- hanky panky. When he used those words, what he's referring to, he was satisfied there was no manipulation going on in the trading of the shares of the company, nothing at all to do with the accounting.

Q Do you recall being questioned by Mr. Velie about certain drafts of the proxy statement and asking some questions as to when you had occasion to rewrite these footnotes that appear in Government's Exhibit 17?

A Yes.

Q You remember he asked you about an August 14 draft and an August 15 draftof the proxy?

A Yes, sir.

Q What is Government's Exhibit 17?

A This is a document on which I had been working, document with which I was making my review as I discussed in my direct and cross examination, which I personally wrote on top at that point master draft, 8-9-69, master proof, 8-9-69, August 9, 1969.

Q Is that the document on which you made the changes?

A Yes, it is.

Q That is the August 9 draft?

A Yes, this is the original of the changes.

Q Do you remember Mr. Velie made some reference to whether or not Mr. Otkiss had that draft? I show you your Exhibit U, which I believe you testified contains your handwriting at the top, J. S.

Would you read that part of it, please?

A "J.S.", meaning to Joe Scansaroli.

"I gave this information to Mathews this morning, 8-4-69."

Q What is that, sir.

A It is a listing of instructions given to Mr. Mathews at White and Case at his request as to who should receive copies of the proofs of the proxy.

Q Who was the second person named on that list of instructions to receive a proof?

A Lee Otkiss, PMM Philadelphia.

Q Do you recall, sir, that Mr. Velie asked you some questions about APB 9? Do you recall being asked some questions about that?

A Yes, I do.

Q Do you recall specifically he asked you some questions about whether or not APB 9 says anything about setting forth separately on an income statement any extraordinary items? Do you recall being asked questions in that area?

A Yes, sir.

Q Let me put before you, sir, Government's Exhibit 25, the proxy, page 21.

Would you tell the ladies and gentlemen of the jury what that is?

A It is the statement of -- it is the consolidated statement of earnings of National Student Marketing Corporation and subsidiaries for the five years '68 plus the five months ended May 31, 1968, and '69.

Q With regard to the statement of earnings for August 31, 1968, is there any extraordinary items set out on that statement of earnings?

A Yes, there certainly is.

Q What is that item?

A Reduction of deferred tax provision as a result of net operating loss carried forward.

Q What is the amount?

A The amount appearing in the 1968 column is $188,750.

Q Mr. Velie asked you about some of the provisions of the same document.

Tell the ladies and gentlemen of the jury what the last note to APB 9 says?

A "Unless otherwise stated, opinions of the board are not intended to be retroactive, they are not intended to be applicable to items."

Q You were asked certain questions, sir, concerning the fact that there came a time when you determined that the provision relating to this deferred tax item which had been calculated in May was at least in part in error.

Do you recall being asked those questions?

A Yes, sir.

Q When was this determined as best you can recall?

A I believe it was in January of 1970.

Q I put before you Natelli Exhibit P in evidence, which Mrs. Raimondo identified as the August 31, 1968 tax return.

Do you recall that testimony?

A Yes, sir.

Q Looking at that, does that reflect a tax loss carry forward?

A Yes, sir.

Q What is the total amount of tax loss carried forward reflected on that return?

MR. VELIE: Your Honor, I object to this. We didn't go through the tax return with Mr. Natelli. He went through it on his direct. He is simply going through his direct again.

MR. MARTIN: I did not go through it on his direct, your Honor.

MR. VELIE: It is simply not responsive to any cross examination.

THE COURT: I am not sure about that.

But one thing that puzzles me, Mr. Natelli, I thought you stated that you had nothing directly to do with this that you can recall at the time, or was I erroneous in

my --

THE WITNESS: In May of 1969.

THE COURT: Yes.

THE WITNESS: No, I never said that, sir. I think that pertains to August 31, 1968.

THE COURT: I beg your pardon. You did have something to do with preparation of tax matters in May of 1969, is that the fact?

THE WITNESS: I believe -- I am not trying to be difficult, your Honor, but in terms of tax matters can I explain it wasn't the preparation of this tax return I had anything to do with in particular, but the discussion of and decision made as to the retroactive tax adjustment, yes, sir, I was involved in that.

THE COURT: You say that you did have some discussions?

THE WITNESS: Yes, sir.

THE COURT: You remember I asked you about this yesterday because I was concerned that you didn't understand the thrust of Mr. Velie's question?

THE WITNESS: And as it turned out, your Honor, his questions were restated because there was confusion, which I think you brought out on your questioning of me.

THE COURT: That was my only purpose, for better

or worse.

What I am trying to get clear in my mind now is this. I am not blaming you. This may be my fault or it may be Mr. Martin's fault. I just don't understand the thrust of what is going on here. Are you now trying to tell us that in May of 1969 you did have occasion to look at some of these tax figures and discuss them with somebody?

THEWITNESS: Yes. I believe that has always been my testimony, your Honor.

THE COURT: Fine. Was that somebody Joseph Scansaroli?

THE WITNESS: Yes, sir, among others.

THE COURT: All right. Mr. Martin, perhaps you could help clarify whatever it is you want to bring out, and I certainly will permit it as long as it is in this area.

BY MR. MARTIN:

Q You just testified, sir, that the tax loss carry forward on that return was $613,000, is that correct?

MR. VELIE: Excuse me, your Honor. I object to this. There is no basis laid. He has not testified that he ever stuck his nose in that tax return, looked at it or discussed that particular figure with anyone.

THE COURT: I am inclined to agree.

Let me put it to you, Mr. Martin. I don't see

what this has to do with our case nor do I see what it has to do with your client's testimony, now that he has clarified it, and we are not interested, the Government does not accuse anybody of misstatement in those tax returns of NSM.

Now, I insist that redirect, of all times, is not the testimony to get into this matter. If you want to ask him about his discussions and what he did in May of 1969, I say for the second time I will be glad to permit it, notwithstanding Government counsel's objection.

MR. MARTIN: Your Honor, what I am really trying to get to -- let me try it another way.

THE COURT: Please do. I just think going through these tax returns, which he himself admits he didn't prepare, I assume -- don't you?

THE WITNESS: Yes, sir, correct.

THE COURT: I don't think it is profitable for him or for you.

Q You say that there came a time in January 1970 when you discovered that an error had been made in May, is that correct?

A Yes, sir.

Q Did you at that time review the tax returns?

A Yes. I believe at that time that there was discussion as to how this could have happened and in the course

of that discussion there was reference to the tax returns, yes, sir.

Q Looking at that tax return, would you tell the ladies and gentlemen of the jury what the error was that you discovered in January or February of 1970?

A What the error was?

Q Yes.

A We discovered that the error was that one of the elements representing the difference between the income for financial statement purposes on the company's books as compared to the tax basis income was omitted from the calculation of what the deferred tax provision should have been.

Q What was the provision that was omitted under consideration?

A The item omitted was an amount relating to deferred charges, which for accounting purposes, for financial statement purposes -- excuse me. These charges related to the so-called per inquiry programs, and if you recall, when we discussed that, these are the costs relating to the per inquiry programs that the company would accumulate before the programs were put forth on the campus, and then for accounting statements these would be maintained as deferred charges, which are assets for accounting purposes, and then gradually expensed into the statement of earnings as the

income from these programs would be coming into match income and expenses for that particular type item.

Now, for tax purposes it is permissible, if a company chooses to so report, to take these expenses immediately as an expense in the year that the expense is incurred, and that is the basis upon which NSM had been recording its tax basis income for sometime.

Consequently, you had a difference arising from that situation which also should have been included in deferred tax calculation and that aspect of it was missed when Carol Raimondo and Joe Scansaroli had looked at this item in May '69.

Q At the time in January or February when you determined that this error had been made in computing the tax credit in May of 1970 did you in January of 1970 have conversations about this with anyone at National Student Marketing Corporation?

A Yes,both Joe Scansaroli, who was there at the time, and Bernie Kurek.

Q Is that the same Bernard Kurek who testified he spent twelve days preparing to testify with Mr. Velie?

A Yes, sir.

MR. VELIE: Your Honor --

THE COURT: Yes. Sustained as to form. We know who Kurek is at this point. You don't have to do that.

Q Do you recall, Mr. Natelli, whether when he was testifying Mr.Velie asked him one question about this tax error.

MR. VELIE: Your Honor --

THE COURT: You can argue that to the jury too.

MR. MARTIN: Nothing further, your Honor.

THE COURT: Thank you, Mr. Natelli.

MR. VELIE: I have just one brief question.

RECROSS-EXAMINATION

BY MR. VELIE:

Q Mr. Natelli, you did tell us yesterday, you don't want to change your testimony, with respect to the fact that you don't restate immaterial items, do you?

A Do you restate --

Q If you have an immaterial change you don't restate the prior year, do you?

A You do not, no.

Q And you restated the prior year, didn't you?

A Yes.

Q It follows from that then that the statement was not immaterial?

A I believe if you look at my whole testimony, I stated why a determination was made to restate and why an eventual decision was made that it was immaterial when all finished.

Q This opinion tells you how to restate,doesn't it, and it not only tells you what Mr. Martin showed you you did, which is to set out a figure in a column, but it tells you you must disclose, doesn't it?

A Yes, and it also --

Q And you didn't disclose, did you?

A We did not give narrative disclosure, yes, sir, that's correct.

MR. VELIE: Thank you. I have no further questions.

THE COURT: Mr. Martin.

REDIRECT EXAMINATION

BY MR. MARTIN:

Q What were the reasons that financial statements were restated in August of 1969?

MR. VELIE: We went through this on his direct and on his cross and it is not raised by the recross.

THE COURT: I agree. This is a matter that has been covered for quite a few hours. No need for that.

You may step down, sir.

THE WITNESS: Thank you,sir.

(Witness excused.)

MR. VELIE: Your Honor, this is something that Mr. Martin brought up yesterday at the side bar. I believe we should come up to hear his application with respect to it.

MR. MARTIN: I would certainly agree with that, your Honor.

THE COURT: I am sorry, gentlemen, but I don't

think I agree. First of all, I didn't hear any such matters at the side bar. What I heard was about another witness.

Do you want to call him?

MR. MARTIN: No, your Honor.

THE COURT: You decided not to. So what we are now concerned with is documents.

MR. MARTIN: Yes, your Honor.

MR. VELIE: Yes, your Honor.

THE COURT: You will have to come up.

Excuse us, Mr. Light and ladies and gentlemen of the jury.

(At the side bar)

MR. MARTIN: Your Honor, what I would offer to do at this time is to read those portions of the endorsements on this indictment reflecting the pleas of guilty of Cortes Randall, Robert Bushnell and Dennis Kelly.

MR. VELIE: Your Honor, what Mr. Martin is going to do is to read the clerk's hearsay declarations on the back of that document. It is not evidentiary in any sense. We have had all kinds of witnesses in the case. This is nothing for the jury. It is not their concern who has pleaded guilty and who hasn't. I object.

THE COURT: I would certainly think that the only

basis I would permit this is if everybody is willing to stipulate the obvious facts, that these gentlemen have previously pleaded guilty and are awaiting sentence. I wouldn't object to that. But reading the cover of the indictment, absolutely not.

MR. MARTIN: That is all I wanted.

THE COURT: If Mr. Velie isn't going to stipulate to it then he isn't going to stipulate.

MR. VELIE: I haven't been asked to sipulate to it. There is an offer to read from the back of the indictment.

THE COURT: I won't permit that anyhow, because I am too familiar with what goes on and that is unfair. There might be a slip of the lip and all kinds of errata creep into those things.

MR.MARTIN: Your Honor, I would ask your Honor simply to take judicial notice of the records of the Court and tell the jury --

THE COURT: I will be glad to if everybody agrees. Gentlemen, now we are getting down to matters which we shouldn't be sitting around here at the side bar dilating about. You are competent practitioners. You don't need a nursemaid. Either agree or don't agree.

MR. VELIE: Why don't you give me a few minutes

to think about it.

(In open court.)

THE COURT: Let's move along, please.

MR. MARTIN: Your Honor --

THE COURT: There is no need to discuss it with me. Either he agrees or he doesn't.

MR. MARTIN: He wants some time with this.

THE COURT: Fine. Let's go on to something else.

MR. MARTIN: Your Honor, there is nothing else.

THE COURT: If you would like me to take a recess, gentlemen, I will be glad to. But it is going to have to be brief.

MR. MARTIN: Mr.Velie said he would like some time to consider the question raised, your Honor.

THE COURT: Ladies and gentlemen, at this point I am going to have to ask you to take the morning recess. I believe it will be ten minutes. If I am wrong I will send in word.

(Recess.)

End 3B

(In the robing room.)

THE COURT: Let's go on the record here.

As I understand it, you gentlemen would all agree to have the Court take judicial notice of the fact that Messrs. Kelly, Cortes Randall and James Bushnell prior to trial pleaded guilty to certain counts in this indictment.

MR. VELIE: Yes, your Honor.

THE COURT: Do you want me to take judicial notice in front of the jury?

MR. MARTIN: And I think we should have the further statement that they have not yet been sentenced.

THE COURT: I am not sure that is terribly relevant because they didn't testify. If they had testified, of course it would be relevant. I just think that it is unnecessary and I don't choose to go into that.

Kurek is another problem, of course.

MR. VELIE: There is evidence on the record.

THE COURT: There is already evidence on the record that he is waiting sentence and that is important. As to those three gentlemen, no.

What else?

MR. MARTIN: Should we at this time, your Honor -- the defendant Natelli on that state of the record, after

your Honor advises the jury , will rest. Mr.Scansaroli I know is going to rest at that point. I believe the Government is resting.

Do you want us to make our motions at this time?

THE COURT: Let's make them now on that representation.

MR. MARTIN: Your Honor, at this time the defendant Natelli renews the motion for a judgment of acquittal in this case for all of the reasons set forth at the close of the Government's case, and in addition would argue that the Government has not established that a proxy is a document that is required to be filed. I believe that the law provides only that you may not solicit it a proxy without a proxy statement being on file, and therefore --

THE COURT: You lose me. I don't understand that.

What are you talking about, NSMC?

MR. MARTIN: That is correct, your Honor. My argument is as follows: We are dealing with the criminal statute. It says it must be a document required to be filed. The securities laws specifically require the filing of certain documents, annual reports, 10K's, things of that nature. There is no requirement in the security law that a company must file a proxy.

There is simply a requirement, provision, that it is a crime to solicit a proxy unless a proxy statement is on file.

Therefore, I think that the statutory basis is not made, and I move to dismiss on that ground.

THE COURT: Do you care to respond to that at all?

MR. VELIE: No, your Honor. I don't think that needs any response.

THE COURT: You never know. Be my guest.

MR.VELIE: Thank you, your Honor. What Mr. Martin has said, it is open season on shareholders when it is time to solicit proxies because somehow the Congress of the United States lets something slip between the stools. This proxy was required to be filed because they were going ahead and soliciting proxies. They went and made false statements in it. That is what this case is all about.

THE COURT: In any event, it seems clear that the company and its accountants at the time in question, in the fall, summer of 1969, believed that a proxy was required to be filed, right?

MR. VELIE: And acted accordingly and filed with the SEC.

THE COURT: The motions of the defendant Natelli

for a judgement of acquittal are denied.

MR. MARTIN: I move to dismiss, your Honor, on the ground that the defendant Natelli has been prejudiced by the undue delay in bringing this case to trial, that we have heard a lot about different recollection of witnesses which arises from the fact that this case is now six years old. I think those differences have been shown to be critical.

For that reason I move to dismiss on that ground also.

THE COURT: Wait a minute. Are you talking about the delay between the relevant times and the filing of the indictment?

MR. MARTIN: That is correct, your Honor.

THE COURT: I see. All right.

Do you want to say anything about that motion, Mr. Velie?

MR. VELIE: I don't believe it needs any reply. The period between a commission of a crime and the filing of the indictment is covered by the statute of limitations. There is absolutely no claim that the statute has run with respect to this crime. I believe that is the long and short of this particular argument.

The record clearly reflects that all of the

delays which have occurred since the indictment have been occasioned by requests of one kind and another of these defendants, further time to prepare or one thing and another.

The Government announced its readiness at the first pretrial conference.

THE COURT: He is not pressing that, post indictment, he is pressing the point between the time of the material events in this case and the time of indictment.

You correct me if I am wrong in this.

MR. VELIE: Your Honor, I would make a more elaborate answer on papers if you felt it necessary.

My unaided recollection is that the statute of limitations is what governs here, absent specific requests or specific problems raised which the defendants have suffered, such as the death of a witness or the like and some bad conduct on the part of the Government.

However, the last time I looked at a question like this was some time ago.

THE COURT: I believe that there's no sufficient evidence that the Government has been dilatory or was dilatory in moving this case on to the Securities and Exchange Commission after their investigations to the Department of Justice and to the U. S. Attorney's Office.

I furthermore don't see any evidence of any persuasive nature that anybody was seriously prejudiced at all by this. Therefore, I deny the motion on those bases.

Mr. Stillman.

MR. STILLMAN: Thank you, your Honor. May I do it from a seated position?

THE COURT: Yes, sir.

MR. STILLMAN: Thank you. Of course, your Honor, I adopt the motions made by Mr. Martin. In addition, of course, I move at this time for a judgment of acquittal now

that all of the evidence is in with respect to Joseph Scansaroli.

I respectfully submit, your Honor, that the evidence clearly shows that a reasonable jury could not find beyond a reasonable doubt Joseph Scansaroli unlawfully, wilfully and knowingly participated in the acts charged in this indictment. I would direct your Honor's attention most respectfully to the uncontradicted fact that Mr. Natelli testified that each and every material decision which forms a basis for alleged criminal conduct, is a decision that he as the man in charge made.

I respectfully submit, your Honor, the evidence overwhelmingly shows Joseph Scansaroli as an employee doing his job to the best of his abilities. I submit that there's no evidence whatsoever that he was the guy who called the shots and, therefore, it just seems to me that it would be just terribly unfair to allow the jury to speculate with respect to him. I don't think the evidence supports it, your Honor.

THE COURT: I must say that treating as the law and common sense requires us to do, each defendant's case taken separately, I believe Scansaroli has somewhat of a good argument here. I would put it a little differently. I think the Government has proved overwhelmingly stupidity and

negligence on the part of that poor man and it may well be that the fact finder would find nothing else but that or, alternatively, that the fact finder will say, as you argue, well, Scansaroli himself continually tried to make clear, and there's some other evidence to support this, he was nothing but a functionary who made no decisions of consequences and left it all up to Natelli, et cetera.

I think either argument factually is supported in the record. There is also a point which I am going to charge this jury that perhaps the fact finder could very well say, well, good, but he was so careless and so negligent and so recklessly indifferent to relatively simple information in consequences that any accountant should know, maybe there's enough here to find the requisite criminal intent as we put it. It is a close question, I think frankly as to Scansaroli, as I see it. Certainly if I were the fact-finder, I would be more troubled with his case for a variety of reasons such as you and I have dilated upon. Nevertheless, I think perhaps there's enough to go to the jury. I'm going to deny your motion.

You join in these other motions that Mr. Martin has made?

MR. STILLMAN: I do, your Honor.

THE COURT: What I will say are of a somewhat more

technical nature. I don't mean to deminish them for that reason. You understand what I'm saying.

I am going to deny those motions.

Now, you remember there is really pending in a sense the motion that the defendants made based upon that decision of Judge Frankle, which I regard as pure obiter dictum, but more precisely perhaps on rule 8 of the rules of this Court and so on, free press, fair trial rule. I will reconsider this if the defense asks me to after the verdict. In other words, I'll hold it open to that extent.

MR. MARTIN: That's agreeable, your Honor. I think that's the procedure we all agreed on earlier.

THE COURT: Now, let me rule on the requests. First the Government's.

With regard to the Government's requests, I am going to charge all of their requests in substance -- I stress and repeat, in substance -- except for the following.

Number 19, I will not charge to this extent, Mr. Velie, simply because I don't single out the defendants alone. I think other witnesses can have an interest too. I am going to go into this, but I am not going to make it so unequivocally center only upon the defendants. So I think in fairness to you I should indicate I will not charge number 19, although I will deal with the subject.

I will not charge number 22. Again, I make the point that this isn't to be the basis of the decision, but I don't put it in quite that lengthy eloquent fashion. So perhaps I should say that I won't charge number 22.

All the others in substance I will charge. Let me point out, however, one interesting little fact which may or may not have occurred to you and Mr. Rakoff. Number 16. I was very much misled by that originally, because none of the cases support what I thought was the thrust of this request. Really all those cases do is support the last sentence, which I am frank to say that I don't consider to be a very good sentence. If I were a jury I would say "run that by another time, will you, Judge."

MR. VELIE: I think this results from running together two requests.

THE COURT: I am afraid so. Let me say this: The title of your request contains the real thrust, as I see it.

MR. VELIE: Yes, sir.

THE COURT: And I agree with you on that.

MR. VELIE: Thank you.

THE COURT: All right. Now we turn to the --

MR. STILLMAN: Your Honor, with respect to this charge number 9 of the Government, the last two sentences of number 9, your Honor, which read "Because of this rule of law I have not permitted the Government" --

THE COURT: No, no. I see your point. I am not going to say that.

MR. STILLMAN: All right, sir.

THE COURT: You are right. I beg your pardon. That's what I mean. You see, it is so hard. You go through these things. I regard them as being helpful only to the extent of the point made. As for the language and the specific ~~sconces~~ sentences, you know, it is ridiculous.

MR. MARTIN: Your Honor, may I just raise one point on the Government's requests.

THE COURT: Which number.

MR. MARTIN: I believe it is in 11 they speak of the question of reckless disregard. Referring particularly to the Eastern contract, it seems to me --

THE COURT: Wait a minute. Hold it a moment here.

Again, I am not going to tie the two together like this. I am going to cite arguments of both sides and simply in another context raise the point that Mr. Velie I am sure, is going to argue, because I think he is entitled to. At least by August 1969 somebody in his right mind should have been very skeptical about the EAL contract. But I am not going to weave it in with this, not at all.

MR. MARTIN: There are two points I want to make clear on that. One is I think this is not a case of reckless disregard because there is evidence that this was a matter considered by Mr. Natelli and he either knowingly came to a decision it was wrong or not. It wasn't a question of something he disregarded.

THE COURT: I am sorry. If you are making this point generally, I don't agree with you. If I were the fact-finder I might, but as the Judge, I am going to charge that portion of request number 11, because I think it is required by the law.

But we are mixing up two things possibly here.

I repeat: I quite agree with you that I am not going into this, connecting up that charge to some specific strand of evidence, like request number 11 asks me to do. I think it is necessary, fair or reasonable.

MR. MARTIN: The only other thing I would ask your Honor to consider in that portion of the charge is the fact that you are dealing here in some instances with unaudited statements, so that I think that as to those statements --

THE COURT: I don't want to get into that, please. I am ruling only now on the Government's requests. I think I have made my position clear.

MR. STILLMAN: I am sorry, sir. I did have a couple more things with respect to the Government.

THE COURT: All right. What is it?

MR. STILLMAN: With respect to request number 11, which the Government says is adapted from Judge Mansfield's charge, I believe that that does not accurately state what Judge Mansfield charged in United States vs. Simon.

THE COURT: Gentlemen, again, in regard to number 11, I am not interested in going into all the exact language. That was what I meant when I started out. Again, I am not going into all this business of Eastern Airlines at this point. I quite agree with you. Judge Mansfield didn't say anything about such a thing, that's right. But neither

would any other judge.

MR. STILLMAN: I am sorry. The fault is mine, Judge Tyler. I am not articulating adequately.

What I am suggesting is that the third paragraph has a sentence that ends with saying "A defendant deliberately closed his eyes to facts he had a duty to see or that the defendant recklessly stated as facts things of which he was ignorant."

Now, in the Simon charge Judge Mansfield at that point went on to say "If you find such reckless deliberate indifference or disregard of truth or falsity the law entitles you to infer knowledge therefrom."

It goes on to say --

THE COURT: Mr. Stillman, please. Maybe you and I don't share the same view of what we are doing here. I happen to be going into that on my own motion.

MR. STILLMAN: All right, sir.

THE COURT: I am only ruling, as I have tried to state three times, on the substance. I am not interested in the exact language of Mr. Velie's requests. I am frank to say I am not interested in the exact language of any of yours particularly. I am interested in the legal points.

MR. STILLMAN: All right.

THE COURT: I quite agree with you that Judge

Mansfield did that, and as a matter of fact, on my own motion, and having checked the Simon charge myself weeks ago, I intend to do justwhat you say. But that is not what I am doing now.

MR. STILLMAN: I didn't mean to do that, Judge Tyler.

THE COURT: What else?

MR. STILLMAN: Those are the only specific items I have with respect to the Government's requests.

THE COURT. Mr. Martin, anything you have overlooked?

MR. MARTIN: No, your Honor.

THE COURT: Now, let us turn to the defendant Natelli's requests.

First of all, you, as has Mr. Stillman, at my suggestion, or certainly I indicated I would be glad to consider them, have certain contention charges. I think I will cover the points. Again I stress I will not go into the evidentiary detail, which I do not think a Judge should do. But the points you hit, the high spots, both defendants, I will so charge, as to contentions.

MR. VELIE: Your Honor, the Government's contentions I am sorry to say are a little bit late, but they will be served during the day.

THE COURT: Mr. Velie, fine, that's good. Don't worry about it. If I don't know your contentions by this time there is something wrong with you and me, which I don't think there is. There may be lots of things that are, but not this.

MR. VELIE: Thank you.

5B

THE COURT: Request No. 1 of Natelli is all right except for the following: I am not going to charge Number 2 of Request No. 1 because I believe it is erroneous for reasons already indicated on the record.

The last phrase in Number 4 I will not charge, with the intent to defraud, because this particular statute I believe doesn't require proof of intention to defraud.

I refuse to charge Number 2.

In all other respects I believe I will charge in substance as you requested.

MR. MARTIN: Thank you, your Honor.

THE COURT: Mr. Stillman, on behalf of Joseph Scansaroli, in substance I will charge Requests Numbers 1 through 8.

I come now to something, Mr. Stillman, that I would have thought you would have remembered as part of my idiosyncratic behavior for many years, including a case or two where you were Government counsel. They were a long time ago, so I don't know.

Take a look at your Request Number 9, dealing with circumstantial evidence. You have requested, quite reasonably, the third paragraph on the first page of that Request Number 9. I recognize that many Judges give that request. I refuse to do so, and I will tell you why.

Years ago I learned that some jurors regard that as akin to the civil burden of proof balancing test and I maintain that no defendant means to request it on that basis.

MR. STILLMAN: Precisely.

THE COURT: I believe as a result of that experience that it is confusing and in fact potentially prejudicial to, of all people, defendants on trial in a criminal case. So historically, for whatever it is worth, I have always refused to give that particular request. Needless to say, you have every reason to disagree, and an exception to you.

I refuse to charge Number 11 for substantially the same reasons, although certainly I will get into inferences and circumstantial evidence.

MR. VELIE: You seem to have jumped over 10, which also deals with inferences.

THE COURT: Yes. I am sorry. I will not charge that because it becomes a balancing test, in my opinion, which is something far below the burden of proof on the Government in a criminal case.

Now, Number 12 I believe is not completely accurate under the law in respect to the matters set forth in Paragraph 2 thereof. However, the error I find comes

in subdivision 1 in that paragraph. The rest in substance I will charge.

MR. STILLMAN: My main concern, your Honor, frankly, insofar as argument is concerned, is with subdivisi... 4. May I take it that your Honor will be charging in substance what I have set forth there?

THE COURT: I am going to charge the elements pretty much as Mr.Velie and the Government requested. They do not include the point that you want to argue, that a report was required to be filed.

MR. STILLMAN: It is not that far. I am really more addressing myself, your Honor, to that part which talks about the way in which the jury should appraise the conduct of the defendant, that is, the question of whether he acted wilfully and knowingly.

THE COURT: I don't argue with that particularly I will not charge Number 4 as you put it because I don't think that the law requires that we have to have proof that he actually knew the report was to be filed. In this case I can't believe that either one of these defendants would ever seriously claim that they didn't know this was going to be filed.

MR. STILLMAN: I have no intention of arguing that, Judge Tyler.

THE COURT: As to the rest, I don't see anything in there wrong fromthe point of view of argument.

MR. STILLMAN: Very well, sir.

THE COURT: Now let me finish this job.

I will charge in substance Requests Numbers 12 - except as heretofore indicated -- 13, 14, 15, except,Mr. Stillman, on the second page of Number 5, I will not charge the last sentence, which I believe is not entirely clear and may be inaccurate as to the thrust of the law.

So just for your own guidance, I will not charge the last sentence.

MR. STILLMAN: Very well, sir.

THE COURT: I will not charge Number 16 because the footnote isn't the only issue inthis case.

MR. STILLMAN: I appreciate that, your Honor. The request of course was addressing itself to it, it being the footnote, and I am not by that request claiming that there is no other element to the charge.

THE COURT: I will get into the point. I read it as being a flat statement that the issue, that is, the only issue, is the footnote phrasing, and I don't believe that is so at all.

MR. STILLMAN: I think your Honor is right, that it is not artfully enough phrased.

THE COURT: I certainly think that the rest of it in substance is all right.

I will charge Number 17 in substance, Number 18 in substance.

MR. STILLMAN: Your Honor, with respect to 18 - forgive me for interrupting you -- frankly, the word that I am most concerned about in Request Number 18 is the word "participant," to be distinguished from the word that the Government likes to use, "accomplice," and I would urge your Honor to use the word participant.

THE COURT: I am not going to necessarily use the word participant. If you want me to do that, exception to you.

MR. STILLMAN: Thank you, sir.

THE COURT: Number 19, I refuse to charge the first paragraph of that. I will charge the second paragrap to the extent I have already indicated because the Government joins in that request. There is no charge that these men deliberately defrauded anybody and there is no requirement, of course, on the Government to prove that. So the second paragraph of your Number 19 I will charge in substanc

Request Number 20 I don't understand to have any applicability and I am not going to charge Number 20.

Number 21 of course I will charge. I regard

Number 22 as the same and repetitive and therefore I don't have to say anything about that.

Number 23 I will charge in substance, Number 24 I will charge in substance.

I will not charge Number 25.

Now, I think that covers everything, unless there is a question.

MR. MARTIN: Just one question, your Honor, on time. I would like about five minutes to visit the plumbing and line up my materials for summation, so I don't go floudering around.

THE COURT: Yes.

MR. MARTIN: I will probably run about an hour and a half.

THE COURT: All right.

MR. MARTIN: Your idea would be to conclude even if we go a little past the luncheon break?

THE COURT: I am afraid we are going to have to.

MR. MARTIN: Fine. The other thing is I am going to refer to two blowups of pieces of evidence that I have had prepared. I will show them to Mr.Velie now. One is simply the statement of earnings page of the proxy over which I have put from the transcript the testimony of Mr. Dingwall.

THE COURT: I think you better do what you said you were going to do first and then we will get to those matters.

MR. VELIE: Your Honor, I am sorry that this is late, as it is, but I do have very brief contentions charges, and if you will accept them I will serve them now.

THE COURT: Thank you very much.

MR. VELIE: Thank you, your Honor.

(Recess.)

End 5B

(In open court; jury absent.)

MR. VELIE: There is one very brief matter, your Honor. The defendant has had sitting in the courtroom wrapped up in paper various charts that they had prepared. Despite the fact that I have requested an opportunity to review them before they used them, that opportunity has been denied up until two minutes ago when I see that this particular chart, which Mr. Martin wants to spring on the jury, contains a portion of a sentence taken out of context plus --

THE COURT: In any event, it is not in evidence. At this late date I don't propose to permit this kind of thing for that additional reason. I think that is very unfair and very distorting. I don't understand you.

MR. MARTIN: Your Honor, those are two pieces of evidence that are in evidence. That is a direct quote from Mr. Dingwall --

THE COURT: I didn't say otherwise, Mr. Martin. We can't have any last minute surprises like this, Number 1.

Number 2, it is not in evidence.

MR. MARTIN: I was waiting until the Government rested.

THE COURT: The Government rested days ago. I

don't follow you. In any case, this is not permissible in summations. I am not going to permit it. You can argue the point, of course. We don't need a chart for that

All right, let's bring the jury in.

You want to mark that for identification purpose

MR. MARTIN: Yes, your Honor. We can do that at a later time.

THE COURT: All right.

Mr.Martin, one thing that I overlooked. Perhaps it came in at noon yesterday. I apologize to you. You submitted an additional request.

MR. MARTIN: Yes, your Honor.

THE COURT: Number 8. I will charge that in part. However, I will not go into the detail. Beginning with the sentence "as to the unaudited statement," through the bottom of that page, I will not charge, the rest I will.

MR. ~~FINE~~ MARTIN: Fine, your Honor.

(Jury present.)

THE COURT: Gentlemen, though I know this fact, the jury does not. Would you please tell the jury that you have rested?

MR. MARTIN: Your Honor, I would if you would advise the jury of the other matter that we had raised.

THE COURT: That is correct. Thank you for

reminding me..

The attorneys for their clients in this case, Mr. Light and ladies and gentlemen, have asked the Court to take judicial notice of the fact, and it is a fact, that prior to this trial Mr. Cortes Randall, Mr. James Bushnell and Mr. Dennis Kelly, who are named in this indictment, pleaded guilty to certain counts in this indictment in this court. I think that covers it.

MR. MARTIN: That does, your Honor.

The defendant Natelli rests.

MR. STILLMAN: Mr.Scansaroli rests, your Honor.

MR. VELIE: Your Honor, the Government rests.

THE COURT: All right.

MR. MARTIN: So we observed the niceties, your Honor. We will now renew the matters that we took up with your Honor in the robing room.

THE COURT: And I will make the same rulings and response to those various motions and applications which I made heretofore as you put it in the robing room.

Now, ladies and gentlemen, we come to the portion of the case where we will hear closing arguments, and the procedure we will follow in this case will be we will first hear from the defendants and then last from the Government, Prosecutor Mr.Velie.

[PAGES 2154-2263 DELETED]

Tk 1A

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United States of America

vs.

74 Cr. 43.

Anthony M. Natelli and
Joseph Scansaroli

New York, New York.
November 13, 1974 - 9:30 A.M.

(Trial resumed.)

(In open court; jury present.)

THE COURT: Good morning, ladies and gentlemen.

Mr.Velie.

MR. VELIE: Thank you, your Honor.

May it please the Court, Mr. Light, ladies and gentlemen of the jury:

Yesterday for just about a full court session you heard a tremendous performance by two highly-skilled, aggressive criminal defense lawyers, possibly two of the best criminal defense lawyers in the city,and no doubt you had to admire the way that they spoke to you,spoke to you about this case. I did too. The fact is that what you heard yesterday was speeches.

You have taken an oath to decide this case on the evidence and not on speeches. I will just give you an example of why that is terribly important. Speeches can raise smoke screens, false issues which cloud what

it is you are supposed to be thinking about, what it is that you are going to have to decide with respect to this case. A perfect smoke screen was one that you heard about at length yesterday I believe from Mr. Martin. He was trying to tell you how Peat, Marwick & Mitchell had been very tough on National Student Marketing, so tough, in fact, it wouldn't let them have earnings when they wanted earnings, and so on, so tough that in May and in July the finance committee of National Student Marketing met and said, "Maybe we ought to fire the auditors, they are not acting aggressive enough."

What does that prove after all? Just think about it. The fact is National Student Marketing was a company in a lot of trouble. They had been juggling the books, as you have seen. They had been performing frauds on everybody. They had ~~not~~ no real sales or earnings. They needed aggressive accounting and when it came to the ~~pitch~~ pinch they got it because after the May meeting and after the July meeting these two defendants went to bat for that company and put out that fraudulent proxy statement, pulled them out of a hole, allowed them to acquire four more companies. So that is what that proves. You should be very careful when you listen to lawyers' speeches that you are not fooled by listening to something that they say, that they have pulled out of context, given you the wrong date, maybe misled you. That is what

smoke screens are.

I could stand here and clear away smoke screens, field half truths, for another three hours, just answering everything that they said. But I am going to trust your judgment to pay attention to the evidence and to the fundamental issue in this case.

Now, it is important to do that because I think you have probably seen that the defense approach in this case, like the defense approach in just about any case that a juror would see, would be something like this: You have watched here for three or four weeks now as the evidence came in and you have probably learned a lot about the rules of evidence while you sat here, only one witness at a time, only one question at a time, one answer at a time, one document at a time.

The case gets built up brick by brick just like a building. What the defendants are saying here, this is a brick, that is no building, here is a little brick, that is no building. They are pulling out little bricks and keeping you from focusing on what the case is really about.

I have a suggestion for you and I hope you will accept it. When you go to work on this case a couple of hours from now and go do your important work of trying to decide this case, I want you to adopt this approach.

Try to keep your eye on the ball, what the real issue is inthis case, because what the issue is, what this case is all about, is what these defendants knew in contrast in complete contrast, to what they said in that fraudulent proxy statement.

Remember, the proxy statement was prepared late in the proof, finally prepared in August and September, and it was filed in late September, and by that time the proof in this case is that these defendants knew that that company was a loser.

When I say a loser, I mean a loser, because the undisputed proof in the case shows that without all the fancy accounting for unbilled accounts receivable which you found out was fraudulent in this case, without unbilled accounts receivable there is this tremendous loss, with unbilled accounts receivable they are able to show a gain.

We don't have a chart to show you the same thing for the May period, which is the later period. This is for the year ended 1968. There is another accounting period in the case, a period that ended in May of 1969. But we have Mr. Dingwall's testimony and it is uncontradicted. Without unbilled accounts receivable, even in May of 1969, even though they had gobbled up all those new companies, they still had a loss if they didn't have these phony unbilled

accounts receivables on the books. This company was a thorough going loser. The defendants knew it and they didn't tell anybody.

Point Number 1.

Point Number 2, the defendants knew by the time they prepared the proxy statement that the company was not only a loser but the company was in the business of defrauding people, acquiring companies when they didn't have any earnings, and they knew this, as you could see, because the defendants saw them doing it too. They were juggling the books. Not once, not twice, but three different times. They would pump the earnings of a period that had already ended by all of a sudden coming up with these unbilled accounts receivable and saying, "Well, let's count that as earnings for the period two months ago."

They did in 1968, $1.7 million. They did it again with the Pontiac commitment, $1.2 million in sales. They did it for the third time with the help of these defendants at the Pandick Press at three o'clock in the morning when it is time to put out a proxy statement and tell people what the company had earned and they are printing it up.

All of a sudden there is a hole in the earnings because Pontiac has been written off.

Magically, magically, up comes this Eastern Airlines contract.

It is supposed to be for a period ended two months before. Nobody ever heard of it.

They just plugged that right in.

They knew that this company was juggling the books.

They knew it and they didn't tell anybody. They hid the truth.

That's what the case is about. If you approach the fundamental issue in this way, keep your eye on the evidence, keep your eye on this issue, you should have no difficulty with the case. Perhaps you will recall that I told you in the opening fundamentally this is a simple case, and it is. There has been a lot of proof. That doesn't meant that it is a complicated case. There have been some complicated explanations by the defendants, but that doesn't make it a complicated case. The case is as simple as this: These people knew that that company was no good and they went and told the people who were going to rely on those statements something completely different, something completely false.

Chronologically the proof in the case is really a very simple story also, because you will remember Peat, Marwick and Mitchell and with them Natelli and Scansaroli come on the scene in August and September of 1968.

The first thing they set out to do is to audit the company. During the course of the audit it becomes obvious that the company is going to have a loss. You don't have to take my word for it. Government's Exhibit 1, Mr. Kurek prepared a schedule, the evidence shows that it is dated On October 2, Government's Exhibit 1 in evidence.

The schedule shows that all the way in October, after the year had ended in August, the company and its own

records was going to show a loss. No secret to the defendants because in their own work papers, in Government's Exhibit 4C, there are trial balances identified here by Mr. Oberlander and Mr. Johnston. I don't have to show them to you. You will have all these for yourself. Those trial balances show that before anybody heard of these unbilled accounts receivables therewas a good size loss in that company.

Well, half way through the audit, in October, after ~~the loss~~ it looks like the company is going to have a loss, out of nowhere, out of thin air, $1.7 million of so called sales. And it is not just the fact that they come up late. To be sure, sometimes there are going to be post period adjustments. But these things just came out of nowhere. Nobody had ever heard of them. There wasn't a record anywhere indicating that the company had spent one red cent doing the business that the company said it had back there in August, not a single record, not a contract having anythi to do with August.

Thereweren't any records whatever, and in fact they didn't even have any binding contracts to represent these so-called sales.

And again, you don't have to take my word for it. It is expressed in Government's Exhibit 3. Mr. Scansaroli

noted on or about October 26, when he dated this page, "Under this method extra caution should be used because there is no legal binding contract."

Again, Mr. Scansaroli in the grand jury testified in the grand jury, and you will recall that it was read and that it was read to him, the situation was touch and go, the salesmen might lose the business, the salesmen might lose the business because the advertisers might send it someplace else.

All of this in October, in October, two months after the year had ended. Mr. Scansaroli knew that there were no sales, no sales at all, the situation was touch and go.

Again, in Government's Exhibit 7, a meeting in December, Mr. Natelli says by August 31, 1969, that is, by next year, he is saying to the company, he wants all contracts or commitments to be firm enough to confirm in writing. It is right here in this exhibit. What that means is he knew that the 1968 contracts were not firm enough, you couldn't confirm them in writing, they might just evaporate, they might lose the business. That's what he knew. That's what the documents show.

Again, Government's Exhibit 16. In June Mr. Natelli is speaking. You don't have to take my word for it

or Bernard Kurek's word for it. There is a transcript of the conversation these men had. It is a partial transcript, but there was a secretary taking it down, doing the best she could.

In this exhibit Mr. Natelli repeatedly complains "$3.3 million of unbilled accounts receivable are sitting unbilled. You can't collect them, you can't sue on them. I doubt if you have a case."

There is simply no question back there when it was happening the defendants took an awful risk without disclosing that they were doing this to anybody in booking these so-called sales when there were no contracts, no documents, an understanding, a clear understanding on their part that the salesmen hadn't even gotten the business.

So clear an understanding, in fact, that it is reflected in the work papers in Exhibit 4C, which I believe I have here, a note from Mr. Natelli to Mr. Scansaroli and an answer, "Can you find out if the salesmen are even entitled to their commissions." Answer, "No they are not."

The salesmen aren't even entitled to their commissions. What kind of sales are these after all?

Well, Mr. Stillman made a wonderful argument to you yesterday. He said people make a mistake. That doesn't mean that they are going to go commit a Federal crime after that.

You can evaluate that argument for yourself. But evaluate this mistake for yourself, because this wasn't just a simple mistake. This was complete and utter indifference to doing an honest job of reporting what that company had done in 1968, complete and utter indifference to being professional about their work.

It was so outrageous, in fact, to call these things, these so-called commitments, sales and earnings that Mr. Scansaroli when he testified before you here, changed his story, went back on his oath, changed a version that he had previously given under oath and denied that the situation was touch and go and tried to tell you that he thought that they were binding, despite all these documents and despite all his prior testimony. That is how powerful this mistake was, and the way he still views it.

He can't, you may find, see his way clear to telling you the truth about it.

And Mr. Natelli, who was supposed to be supervising all this, what's he tell you about? He didn't bother to read the work papers which are just about this thing, may' 30, 40 pages. He would have found out all these things. He tells us he didn't look. He tells us he didn't ask Mr. Scansaroli. He tells us Mr. Scansaroli didn't tell him thes things. He didn't know.

Well, the proof shows that in Government's Exhibit 7 and Government's Exhibit 16, Mr. Natelli knew. That's in Government's Exhibit 3, where he should have known if he didn't; picked up the document and found out for himself.

Now, this was a company, Peat, Marwick and Mitchell Company, which knew how to do an audit. You have seen some evidence here of how an audit ought to be done; the audit, for example, by Mr. Johnston in 1969 after the proxy had been prepared. Mr. Johnston confirmed every singl contract, he confirmed every one of them in writing, and he kept direct control and, this is critical, direct control.

Mr. Johnston was so careful that when he mailed out the confirmations to the people he was trying to get con firmations from, the clients of National Student Marketing, he wouldn't even let anybody mail them. He kept control of the mailings. He got them back in self-addressed mailers.

He kept proper records of what he had done.

In complete contrast, what did Mr. Scansaroli do? When he got on the telephone to check with people, he s... he was going to confirm these commitments. He doesn't even know who he was talking to. Apparently he didn't even pick up the phone and ask who am I talking to? What connection d... you have with National Student Marketing? How in the world can you tell me anything about these confirmations that I'm seeking?

Because incredibly that man picked up the phone and talked to the printing shop and says that he thought he was talking to the advertising agency. He didn't record in his work papers the names of the telephone numbers thathe called. He let the salesmen dial the telephone for him. He simply assumed without checking that the earnings that he was recording for 1968 had been earned back in 1968. He did nothing to check, despite the fact that the only records of these things were hastily prepared forms, all of them dated October 17 and 18.

He didn't even look for a written proposal to the Clairol Company as some evidence that National Student Marketing had done something for Clairol, and you remember that's a half a million dollars of sales and earnings that h... went and put into the books two months after the year had

ended and he didn't so much as lookfor the written proposal. He didn't check with Arthur Andersen, the prior auditors. He didn't check with Michael Sullivan, the accountant who was a recently as the month before had been working on these books.

He put into his papers something which he says is a contract evidencing $138,000 worth of sales for 1968. It is the Syntex letter commitment.

It must be apparent to you he didn't read it. That thing is dated in October. It speaks about a proposal made in October. This is two months after the year ended and it is not a commitment for anybody to do anything. It doesn't require National Student Marketing to perform any services. It doesn't promise National Student Marketing one red penny. It doesn't mention ary money amount at all.

In any event, it has a money back guarantee in it. Yet he includes this as $138.000 of 1968's earnings.

So what kind of a mistake is this? Look for an analogy. Look for anotherprofession, say a doctor. If a doctor diagnosed a patient with kind of an indifference to finding out what kind of disease the patient had and then prescribed drugs for him, powerful drugs, and then the patient died, that doctor would have a problem and he would know it. He would be afraid he might lose his certificate.

That's really what we have here because here, to keep with that analogy, the patient died. Within a period of months o the $1.7 million that these guys pumped into National Studen Marketing after the fact, changed that loss that they had in a gain of the $1.7 million, within months a million dollars was written off as worthless. That's not all.

They knew that the balance could not be collected. In fact, they knew that there were real problems with many o them.

May I have chart 15, please?

You look at chart 15, just this portion of the chart now. You will see that on May 22 Joseph Scansaroli wrote down in the work papers all of these contracts, all of these amounts and knew that they would never be collected That's on May 22, right at the very same time that he knew an additional million dollars was being written off.

Only two weeks after May 22 when all of this bad news hit home with a crash, a million dollar write off, the other contracts no good, no collections on any of the others within weeks after that, two weeks afterward, Mr. Natelli has a conversation with Mr. Kurek. It is in Government's Exhibi 14. Mr. Kurek testified about it.

The matter was so important to him that he sat down on that very day and wrote a memorandum to Mr. Randall. This is important because this thing was written on June 3, 1969, the day that that conversation was had. There was no lawsuit then. There was no investigation then.

Mr. Kurek had no motive at all to do anything other than to tell Mr. Randall that terribly important thing that happened that day that Tony Natelli told him, Kurek: The accountants are scared, they know these contracts make or break the company, they know these contracts aren't being performed, they are afraid that if something goes wrong they are going to lose their certificates and their careers are at stake. It is right here in this exhibit.

You send for it. You read it. You will find it.

Incredibly as you may find, Mr. Natelli somehow or other can't remember ever saying these things to Mr. Kurek. Fortunately Mr. Kurek wrote it down so we don't have to worry about Mr. Natelli's denial.

Mr.Scansaroli equally incredibly you may find denied that he -- denied flatly and repeatedly that he ever said any such thing to anybody. It must be obvious to you

who Mr. Natelli is talking about, the accountants under him. The accountant under him was Joseph Scansaroli. Joseph Scansaroli is the person who audited personally all these $1.7 million contracts which are turning out to be utterly worthless just months later.

It is obvious who Natelli is talking about. Scansaroli denies he ever said any such thing.

Even Mr. Natelli had to acknowledge that Mr. Scansaroli said it not once, not once, but repeatedly and he said it when the Ron Michaels contracts, the million dollars of contracts, were being written off, right in this May period. That is when Mr.Scansaroli was saying it despite the fact that he denies it here.

Well, the result of this motive, this fear that they were going to lose their certificates gave rise to the criminal non-disclosures in this proxy statement which we are talking about in this case. Again, pleasse bear in mind what they knew in contrast with what they said.

There is no doubt at all that Mr.Scansaroli knew that a million dollars of contracts were written off because if you were to look in Government Exhibit 13, which is the proxy binder, you will find -- Mr.Scansaroli identified them for us -- his own handwriting, Mr. Oberlander

identified it as well -- Scansaroli's handwriting actually writing off $750,000 of the $1 million.

He pasted into his book or stapled into his book in other places the balance of that million dollar writeoff, all in this little period in May. So Mr. Scansaroli is wrapped up in these documents. He knew a million dollars had been written off. Mr. Natelli knew it as well.

Government Exhibit 16, which I have already had reference to, right here, it is the meeting of June 9, 1969. Mr. Natelli's meeting with Mr. Randall. In that meeting Randall tells him approximately a million dollars of contracts have been written off. Here is a transcript of the meeting. You send for it. You read it. You will see it for yourself.

Mr. Natelli acknowledges that he knows a million dollars had been written off. He says he knows the balance are uncollectible. He knows what the problems are.

This is on June 9, 1969, right here in this transcript.

Once again, Mr. Natelli somehow or other can't recall the things he said that day. We have a transcript. The stenographer took it down. She had no motive to deceiv anybody. She did the best she could to write down the

important things that were said that day.

Well, the proxy statement is Government Exhibit 25.

It has in it a passage about 1968 earnings. 1968 earnings appear in the earnings statement. They are also broken out especially for people to read about in a footnote. The footnote we are talking about is the footnote which is charged as being false in Paragraph 3 of the statement.

With respect to this proxy statement, these defendants knew what the proxy statement was for. It is a proxy statement so National Student Marketing can acquire an additional four companies, Mr.Frommer's company, the Mar-Clay Company, a company called Mailbag, and the insurance company, Interstate. That is all this proxy is about

They are going to go out, show people what their earnings are, and then acquire those companies in exchange for National Student Marketing stock, and Mr. Natelli and Mr.Scansaroli know Mr.Frommer and these other people are going to read these statements and they are going to rely on them, and Mr. Frommer and these other people are going to think that this is true.

Look what they say. They report the earnings as originally reported for 1968, approximately $5 million, and not a whisper anywhere of what they know, we proved that they knew, over $1 million of 1968 sales originally reported had been written off as worthless.

Instead what these defendants did rather than disclose it in any way was they buried it. They took every penny of loss resulting from that $1 million writeoff, all the sales that had been written off, all the earnings that had been written off, and they tucked them away where nobody would ever find them.

Three-quarters of a million dollars of National Student Marketing's losses were subtracted from the pooled companies' line.

And you remember what that is. National Student Marketing lost the money. Then they went out and bought some other companies and what has happened here is these

defendants have subtracted the losses from companies that never lost the money and not from National Student Marketing. The result is nobody will ever find out, nobody will ever find out, the $1 million has in fact been written off.

In short, what the defendants did was they doctored the books. You can find that they went actually to great lengths to deceive here.

This chart you have seen several times in the proof. This chart has been shown several times in the proof and the interesting thing about it is that it shows just what a thorough going job of covering up was done here, because after Mr. Scansaroli, as you may find, subtracted $678,000 from the work papers from the pooled companies' line, leaving this as a false and only partially true footnote, Mr. Natelli, with thorough-going carefulness, takes the remaining $21,000, the last little blotch or spot, and wipes it up, subtracts it from the pooled companies himself personally. They really went to great lengths.

Now, I have said that it was Mr. Natelli that you may find who did the subtraction of the $678,000, and here is why. Not only was Mr.Scansaroli responsible for those figures, as his grand jury testimony and the proof by Mr. Buck and Mr. Johnston showed, but we actually have a schedule in which the line, the pooled companies' line,

is made up.

Here in the 1968 foot note are each of the pooled companies in a column and the material that was in fact subtracted from the pooled companies instead of from National Student Marketing. This is the work paper. You can send for it. You will find it at Page 2530 of Exhibit 13. It is Mr.Scansaroli's work paper.

Now, Mr. Natelli wasn't very shy about this in the grand jury. He said it probably, as you heard his grand jury testimony read, it was probably Mr.Scansaroli or possibly somebody else.

You consider this and you will know who did it. It is obvious that it was Mr. Natelli polished off the job himself, subtracting every last item from those pooled companies' lines, and he had to know that Mr. Scansaroli had subtracted the first part or he wouldn't have done what he did.

Now, you have heard a lot of talk here, especially from Mr. Martin, about professional judgments. Sure, professional people like accountants make judgments every day, and it is not every time that they make a mistake that they get blamed or they are scared.

A good example of that is when a doctor has a patient and the patient dies. You don't go and prosecute

the doctor just because his patient died.

But it is quite another matter if you catch that doctor at three o'clock in the morning down in his cellar burying a fresh corpse. That is something else.

The Government suggests that the burial of those losses is exactly analogous and that is what these people have been caught doing.

Just think about it. You can sit there in the jury room and think from night until tomorrow morning and see if you can come up with any innocent explanation for subtracting one company's losses from another company knowingly without disclosing what you have done. In fact, the Government submits there is no innocent explanation.

You heard Mr. Buck testifythat there is no warrant in accounting, that it is improper to subtract one company's losses from another company. Y our common sense tells you the same thing.

The defense called at least seven, by my count, at least seven accountants, including two from universities, Joe Scansaroli's old teacher and the gentleman from Howard University. Not one of them had one kind word tosay for the practice of subtracting one company's losses from another company.

There is no excuse for that.

They had to know that it was wrong.

They do give an excuse, however, saying that there was a tax credit.

You are entitled to find that explanation incredible, phony.

First of all, the defendants can't even get their stories together about this tax credit. Mr. Scansaroli told the SEC that when the tax credit was discovered as an offset to the writeoffs back there in May of 1969, when they discovered that they had made a mistake in the taxes, it was time to come up withthe new tax credit, he tells the SEC under oath that he and Mr. Natelli computed it, and he says there are work papers, only he can't find them.

Now from the witness stand he tells you no, he didn't do it, Mr. Natelli didn't do it. He suggests in part maybe nobody did it, and there are no work papers, and then he tells you that maybe Carol Raimondo did it.

If you remember Miss Raimondo's testimony it is clear on this point. She didn't do it. Page 1389 -- this is Mr. Martin questioning.

"Q Did you and Mr. Scansaroli come to in those discussions, a conclusion to that question?

"A Well, I can't say that I can recall this ever coming to a conclusion per se."

The matter is put absolutely clear on the cross examination, page 1396. I asked her:

"Q Did you actually sit down and compute what the new deferred tax number should be for them, is that the work you did?

A I don't have any memory of ever having done that."

Mr. Natelli tells you something just a little bit different from each of those stores. He tells you that there are work papers only now he can't find them.

Well, what about this tax credit. Perfect timing. It comes up at exactly the right time to absorb every single penny of the write offs that they were then making, just the right amount. And when the SEC gets suspicious and begins to inquire all of a sudden, it turns out there is no tax credit in that amount after all, it turns out to be a mistake.

Even if there were a tax credit, it is no excuse for what they have done here. Mr. Natelli had to acknowledge, as he did yesterday, that you don't restate prior years figures for immaterial amounts, and this is a prior year restatement beyond any doubt, the $1 million, the $748,000 taken off the prior year's statement.

And he had to acknowledge that APB no. 9 says that when you make a prior period adjustment you must disclose it. There was no disclosure here.

Your common sense again will tell you why that accounting rule is so. Suppose you wanted to go out and buy a share of National Student Marketing stock and you see something that says earnings, such and such an amount. Don't you want to know that those earnings were made up of the company's sales, of the way it does its business? Wouldn't you be interested in knowing if there were no sales after all but that behind the scenes somebody had taken out the sales, switched it for a tax gimmick, a tax credit arising out of losses? You would be interested in knowing it, wouldn't you?

The next excuse you get is that Mr. Natelli somehow or other cleared this matter with Mr. Otkiss. The Government submits that Mr. Natelli deceived Mr. Otkiss or doubled talked him in some way. Mr. Otkiss if he saw any-

thing, say the footnote which appears over here on the left, and in this footnote even Mr. Natelli had to acknowledge there is a mistake. Almost $700,000 of National Student Marketing's losses are subtracted from the pooled companies line and you can't tell that there has been a $700,000 write off. Instead the only disclosure that Mr. Otkiss gets to see in this footnote is $70,000 with a $21,000 decrease in earnings. No wonder Mr. Otkiss was confused. Mr. Natelli never told Mr. Otkiss that he proposed to subtract three-quarters of a million dollars of National Student Marketing sales from the pooled companies, for the obvious reason. If he did Otkiss, as you may find, would say "You can't do that."

Mr. Natelli told Mr. Otkiss that the problem here of the unbilled accounts receivables was just one instant, this one fellow Michaels who had done something unethical.

But, it wasn't just Michaels. Mr. Natelli knew at that point, as he had said in June in a transcript which we have here, "You can't collect all $3.3 million of unbilled accounts receivables. I don't think you have a case. You can't sue on these things. The whole volume of 1969 business is sitting there unbilled. You have written off $1 million."

Mr. Natelli tells all these things to Mr. Randall. He tells none of them to Mr. Otkiss. He tells nothing at

any time to Mr. Otkiss of the juggling of the books by this company three different times when they came up with earnings to improve the loss for periods which had already ended.

You are entitled to find that Mr. Natelli double-talked or deceived Mr. Otkiss in some way.

The clear example of that is Mr. Otkiss gets up here and says Natelli told him one thing about the Pontiac contract. Natelli said he just wouldn't let it on the books Mr. Natelli tells you that he told Otkiss something quite differently, that he told him the truth of the thing, that it had been on the books and he told him to write it off. Mr. Otkiss apparently was not told the truth of the matter.

Now, these subtractions from the pooled companies instead of from the company that lost it, National Student Marketing, this failure to disclose, this phony tax credit, this is really, you may find, unique accounting, accounting designed to do only one thing, and that is to hide the fact that all those contracts had been written off and were turning out worthless. No doubt that the accounting was unusual.

You heard a lot about Mr. Buck yesterday from both defense counsel. Somehow or other both defense counsel forgot to tell you what Mr. Buck said about the write off

against the deferred tax done by Mr. Scansaroli. He said in his twelve years as a certified public accountant he had never seen anything like it before or since. It was unique and it had one purpose and one design only, to hide the truth of the matter here.

You will be instructed on the law when I am finished by Judge Tyler and the law is plain. When accountants deviate from accounting rules, when they break the rules to do something, it is powerful evidence that they intended to deceive.

You are going to be furnished a copy of the indictment when you go into the jury room. Count 2 appears in several paragraphs. Paragraph 3 specifically charges in this case that the footnote which I have been showing you is false.

It charges that a million dollars, 20 per cent of 1968 sales, had been written off and these defendants didn't say anything about it. You have seen the proof as to that. They knew it and they didn't tell. It is exactly what paragraph 3 charges.

Paragraph 3 charges in addition that the footnote is false because the pooled companies line is understated, National Student Marketing is overstated. That very simply is a result of thatsubtraction that they had no business doing. They subtracted the loss from the pooled companies and understated them. By doing that they left National Student Marketing overstated.

Paragraph 3 of the indictment is just as clear as it can be. You have seen it proved. Bear in mind again when you go to decide this in the jury room what the charge is and what they knew, contrast it with what they said in that footnote.

Now, there is a separate and a second specification of fraud in the indictment. It is in paragraph 4. Thi

has to do with the period ending May 1969, the nine-month period. With respect to that the indictment charges two things.

The company had announced its earnings as about $700,000 for that period. The indictment charges and the Government submits it is proved that there were no earnings at all for that period and that the defendants knew it and failed to disclose it.

Here the absolutely uncontradicted proof is Mr. Dingwall's calculation, that if you take off all these rotten unbilled accounts receivables, there was a loss for that nine-month period. There was no gain at all.

Paragraph 4 of the indictment also charges that the sales for National Student Marketing for that nine-month period were overstated by about $800,000.

Here I want to show you Government's Exhibit 65-15 again, this chart. This summarizes it for you very neatly.

Bear in mind that the indictment charges that they said sales were about $11 million. In fact, it was under 10 million, 5. In other words, an overstatement by about $800,000. This is the figure we are talking about.

This chart summarizes specific sales known to these defendants to be no good at the time they prepared that proxy. About 300,000 of them were specifically found to be no good

by Mr. Scansaroli and by Mr. Oberlander who showed his chart to Mr. Scansaroli.

They knew that that $300,000, and the testimony was that Mr. Natelli was aware of Oberlander's work as well. Mr. Oberlander's work is the great bulk of this. He had access to the work papers.

This was an SEC review designed to find out just this, whether these contracts were any good. 300,000 of them specifically found to be no good, and yet included as components of the figures for that May period. The rest of the 800,000 is the Eastern contracts. You can take that down.

If anything has been proved in this case, ladies and gentlemen, the Government submits that you must have been satisfied beyond any doubt that that Eastern contract was known to be a complete phony when it came up.

The fact is this has to be one of the most ~~single~~ cynical events that you will probably ever ~~here~~ hear about, at 3 o'clock in the morning at the printers plant where they are printing up this very proxy statement, there's going to be a big hole in the earnings becase the Pontiac contract has to come out.

By magic 3 o'clock in the morning the first time it is mentioned the Eastern Airlines contract comes up. It

is supposed to be a contract for the period which ended two months before and yet in the two months between May and August nobody seems to have peeped a word out of it to the controller of National Student Marketing or anybody else who had any business with this matter.

These defendants either had to think that National Student Marketing had gremlins and magic or they were making these things up. Because the same account executive, Dennis Kelly, comes up with this one, came up with the Pontiac one which had to be written off. It is 3 o'clock in the morning. The period had ended. They are printing up the figures.

This was incredibly the third time they knew that the company had pulled this kind of a stunt. The first time, of course, is the $1.7 million. They stick it into the 1968 year after the period had ended.

The second time was the time the company took $1.2 million, the Pontiac contract, put it into the six-month figures and now this time, the third time.

Well, this is probably a good place to speak to you for a minute about circumstantial evidence.

You are going to be instructed that circumstantial evidence is evidence like any other kind of evidence and you are entitled to rely on it just the way you rely on direct evidence. A simple example will show you it is as good if not better than a lot of direct evidence.

Suppose you are working, doing something in one part of your house and you hear a crash from the kitchen and you go running into the kitchen and there is your three-year old boy and he has got red sticky stuff on his face, he has red sticky stuff on his hands and at his feet is a smashed jam jar with jam all stuck in the broken glass. If he tells you, I didn't knock it over, I didn't touch it, it fell all by itself, that is direct evidence.

But the jam on his face and the jam on his hands tell you what must have really happened, that is circumstantial evidence.

It is just like this case, because the defendants have all kinds of explanations. As you may find, they have jam all over their face. That is what the case is about.

This Eastern switch, the single switching of

gab-2

Eastern for Pontiac, described by Mr. Natelli himself as weird, described by Mr.Scansaroli as strange, not a word of this, of what they know, is breathed to Mr. Frommer who is about to part with his company for National Student Marketing stock.

Not a word of it is breathed in the proxy statement so that the Mar-Clay people and the Mailbag people and the Interstate shareholders, 1300 of them could find out what is really the story with this company.

Just to summarize for you the business of Paragraph 4 of this indictment, the period ended May 1969. These defendants knew these specific sales totaling $840,000 had no business being on that proxy statement.

They let it in.

The second thing they knew was that there were no earnings at all because the whole thing was made up of these unbilled accounts receivable which they knew were worthless.

A simple summary of what they knew over their entire period or history with National Student Marketing will show you this: In the entire period that they had been established as the accountants and auditors for National Student Marketing, $3.3 million of unbilled accounts

receivables had been booked by the company, 61 per cent of them, over $2 million, had been written off as worthless A large amount was knownto be absolutely collectible.

That taken with the ones they knew were no good, they knew that the company had repeatedly juggled the books after the period had ended, shows just what they knew. You contrast it with what they said in the proxy statement.

What is the defense here? The defense in the case is, Number 1, Mr.Kurek was lying.

Just think about Mr.Kurek. He was the first witness here. Perhaps you remember him. You remember his demeanor on the stand. Why don't you contrast his demeanor on the stand with that of the two defendants.

Did you notice that Mr. Kurek when he was asked a question on cross-examination gave an answer? Did you notice that Mr. Kurek when he was on cross-examination readily, candidly gave answers even when he knew that it was something the defense wanted emphasis?

He gave away points if he thought that that is what the truth of the matter was.

Mr. Kurek you may find was a thoroughly candid man. He was doing his best, you may find, to tell you the truth.

He didn't change his story. He didn't go back on his oath.

The evidence was, and you saw it, that he had testified in the grand jury and he testified in the SEC.

~~There~~ Their reams of documents with which he was cross-examined and he didn't double back on his story or change his oath.

End 4B

And what was his motive after all. You will remember that Mr. Kurek has pleaded guilty. There is nothing left for Mr. Kurek -- he has pleaded guilty to a count in this case,Count 2 -- there is nothing left for Mr.Kurek to do with respect to the criminal justice system here except the sentence by Judge Tyler. He knows that if he came in here and he didn't give candid and truthful answers Judge Tyler is going to let him have it, but good. That man's motive, the Government submits, was to tell you everything just the way it happened.

In addition, the Government submits that Kurek was fully and completely corroborated. When he told you that the unbilled accounts receivables were booked late, they cfame up for the first time in 1968, in October, two months after the year had ended, you don't have to take his word for it alone. You have Oberlander and Johnston and their work papers that prove it.

When he tells you that there were losses without these contracts, a-gain with it, you don't have to take his word for it alone. You have his schedule,Government Exhibit 1, which I have already shown you. You have Scansaroli's work paper in which he says there is going to be a loss without these contracts.

You have the trial balances of Peat, Marwick, Mitchell to prove it. You have Mr. Dingwall's calculations in the chart which I showed you just a moment ago. Mr. Kurek is fully corroborated on all of these points.

When Mr. Kurek tells you about the meeting of December 9th at which Mr. Natelli says "Next year, fellows, these things will have to be firm enough to confirm in writing," you don't have to just take Mr.Kurek's word for it. There is a memorandum written the very next day for the purpose of telling all the account executives what happened at that meeting.

When it was written there was no lawsuit going on, he had no motive to falsify. He wrote down what he thought was important about that meeting and it corroborates what he says.

When he tells you about the June 3rd meeting at which Mr. Natelli said the accountants fear losing their certificates if anything were to happen, there is Government Exhibit 14, Mr. Kurek's memorandum of the very same day which he wrote to Mr.Randall to put Mr. Randall onnotice of these terribly important facts.

And when Mr. Kurek tells you about that important meeting of June 9 at which Mr. Natelli says "I know that the $1 million were written off," in effect, and he says,

"I know that the rest of them, $3.3 million, are uncollectible, you will never collect them," when Mr. Kurek tells you those things, there is a transcript of the meetin made by a secretary just as things were being said. It is Government Exhibit 16.

You heard a lot of insinuation yesterday inthe arguments by defense counsel. You heard insinuation that Bernard Kurek made up his story in whole or in part to please the Government or in conjunction with the Government

If you believe that for one minute don't even stay in thejury room. Just come on out and acquit, if you think that Bernard Kurek did anything like that.

What is the next line of defense? The comfort letter. Bear in mind that every time an honest accountant at Peat, Marwick & Mitchell gets his hands on the bad news in those work papers things start to happen. Mr. Oberlande when he did his review got so excited that he called Mr. Kurek up at home on a Saturday to tell him about it.

Then what happens? He gives it to Scansaroli, his review, and Scansaroli and Kurek squelch it and it never gets disclosed.

The same thing with the comfort letter, in part, because Mr. Colona and Mr.Johnston get their hands on the books and the records and they start finding things.

They find about $800,000 worth of adjustments. After they find them, after they take a definite position that disclosures have to be made, they call Mr. Natelli at home, where he is sick. They are so excited about it they go and call Mr. Natelli at home.

Well, keep in mind about this comfort letter that it does not tell the whole story by any manner of means. The comfort letter only speaks about certain adjustments. It speaks about certain deferred costs, it speaks about certain capitalized costs, and it speaks about a tiny portion -- I shouldn't say tiny portion -- it speaks about $300,000 of unbilled accounts receivables, tiny compared with the $1 million that Mr. Natelli and Mr. Scansaroli knew were written off in that very same period.

So when Mr. Natelli finds out that they are going to do a comfort letter does he pipe up with the additional information, "Maybe we ought to tell them that they wrote off a million dollars in that very same period, switched it in the dark of night for another one, came up with another one at three o'clock in the morning?"

Oh, no, he doesn't pipe up with that information. He knows that his firm is trying to decide to inform the SEC or not.

You heard Mr.Earle testify. Mr.Earle is a

lawyer for Peat, Marwick & Mitchell. He had to rely on what the accountants told him were the true facts about that comfort letter, and Mr.Natelli didn't tell him the whole story. Instead, as Mr. Natelli had to acknowledge, he and Mr.Scansaroli had a pow-wow and then they go back and report or Mr. Natelli goes back and reports to his superiors at Peat, Marwick & Mitchell "These adjustments are just the result of an honest mistake by the compar

You are entitled to find on the evidence in this case that Mr. Natelli and Mr.Scansaroli set out to deceive their very own company, Peat, Marwick & Mitchell, as well as the shareholders and people who were going to rely on this proxy statement.

In any event, that comfort letter not only had so little in it but it came too late to save Mr.Frommer from being cheated. It came after Mr.Frommer's deal had closed. It came after the Mar-Clay deal had closed. It came after the Mailbag deal had closed. There is absolute no defense at all to the fraud which happened to those people.

The next line of defense here is that somehow or other all these things that the defendants knew and the didn't tell anybody about were immaterial. Now, don't abandon your common sense in a case like this. That is

what jurors are picked for. That is why we take twelve citizens to decide a case like this rather than twelve accountants or scientists or something like that.

You have got your God-given common sense and your experience of everyday affairs. Think about it. You know a lot about National Student Marketing as you sit here today after three weeks of this proof. You know how they juggled the books repeatedly. You know how they wrote on these contracts and wrote them off. You know how they were essentially in the business of trying to acquire other companies, showing them phony sales and earnings that didn't exist and writing them off later after they grabbed up those companies. You know a lot about National Student Marketing. Ask yourselves, wouldyou go and sell your house, your family's business, take the money out of the savings bank, borrow against life insurance, and buy that stock? Ask yourselves if you would do anything like that.

Well, the defendants knew all those things and they didn't warn anybody, and they knew people were relying on this. Mr. Frommer in fact did go out and sell his business for National Student Marketing stock because they never warned him. He read that proxy statement. He felt he was entitled to rely that he was being told the truth. You may find that he got cheated.

5b

The defendants have told you it didn't matter about the 1968 write offs because in 1969 the company was a bigger company. Just ask yourselves whether the defendants aren't trying to pull the same fraud on you that was pulled on Mr. Frommer and on the others, because what the company had been doing was showing phony earnings, acquiring other companies which had real earnings, growing by that system, writing off the phony earnings, and doing it again and doing it again, repeatedly. That is a ~~simple~~ cynical argument because what it boils down to is that fraud is okay as long as it succeeds.

But nobody told Mr. Frommer and nobody told the early acquisitionees that this had happened to them. They might have been interested. They might have wanted to get their companies back. They were never told.

In addition, the argument that the company is bigger in 1969 just ~~false~~ falls of its own weight, because the uncontradicted evidencein this case is as big as that company had gotten, with all the companies that it had gobbled up, it still reported or would have reported a loss if you had taken off all these phony unbilled accounts receivables.

Mr. Natelli himself, in the privacy of a meeting with Mr. Randall on June 9, acknowledged the terrible importance of the fact that these things weren't collectible, and it is here in the transcript, Government's Exhibit 16.

Mr. Natelli said it doesn't matter if you have $45 million or some such number, in sales. It is important that there is $3.3 million of uncollectible unbilled accounts receivables on the books. And it was. He knew it. He knew it and he never told anybody.

I want to remind you again about the defense summations because the defendants in their summations or the defense lawyers in their summations, made some pretty snappy arguments. But those arguments to be good arguments have to be based on evidence, and if you listen carefully to what they were saying what these lawyers were doing was giving you back the stories told by the defendants from the stand, and those arguments are no better and no worse than the credibility of the defendants when they took the stand, took an oath and testified here.

Ask yourselves -- you sat here for three weeks -- ask yourselves, didyou see any witnesses in the case except those defendants bob and weave, change directions, change field like a broken field runner, do anything, as you may find, except give a straight answer to a straight question.

Ask yourselves that.

You saw them with your own eyes. You watched their demeanor when they testified. Ask yourself about Mr. Scansaroli's credibility.

Mr. Stillman stood here yesterday and told you that Mr. Scansaroli represented a breath of fresh air in this case. Well, maybe he forgot or maybe he thought or hoped that you would forget that Mr. Scansaroli is the man that came up here and repeatedly changed evidence that he had previously given under oath before to tell a new story for you.

Now, this is the United States Courthouse. It is 1974. You are jurors with common sense. You don't have to take arguments like that. You can reject them if you don't believe the testimony on which they are based.

You remember the witness and I think you will remember how he changed his story. Mr. Scansaroli told the SEC in 1971 under oath and he told the grand jury in 1973 under oath that he understood that the situation with those 1968 contracts was touch and go, his words, touch and go.

In other words, he knew that the company didn't have those sales, that they might evaporate at any time, that the company could lose the business, there were no earnings, there were no sales. He knew that.

That's so terribly important here in this criminal trial that he got up there on the stand and told you that somehow or other that sworn testimony should be disregarded, you should listen to him today tell you a new story.

And you will recall that Mr. Scansaroli got up there and tried to explain this business of the tax credit we have been talking about, the tax credit which is the excuse for not disclosing some of the write off. What Mr. Scansaroli told the SEC under oath is that when it was time to recompute the tax credit and they discovered this tax credit and they were going to do the write offs he told the SEC he and Mr. Natelli were the only ones who got into it, the only ones who did it. There were work papers. They did their computations.

Well, he came in here and he told you something quite different. He told you that he didn't do it, he told you that Mr.Natelli didn't do it, and he tells you now there aren't any work papers because there didn't need to be any.

Ask yourselves if Joseph Scansaroli's testimony is not utterly inconsistent, at war with the other proof in this case. He tells you that he flatly never told anybody that he was afraid he would lose his certificate. It is inconsistent with Mr. Kurek's sworn testimony, it is inconsistent with the corroborating proof, Government's Exhibit 14, in which Mr. Natelli tells Kurek, "The accountants working for me are in fear of losing their certificates."

It is inconsistent even with Mr. Natelli's testi-

mony, who told you not once but repeatedly Scansaroli had said he was afraid hewould lose his certificate, words to that effect, repeatedly, he said it at the time of the write offs.

Mr. Scansaroli tells you that he wasn't aware that Pontiac and Eastern were being switched at the Pandick Press.

Well, you evaluate that one on its face, because you will recall that Mr. Scansaroli is the man responsible for getting the figures into the proxy statement. That was his job. And that's what they were doing. Pontiac represented figures that either had to come in or go out and so did Eastern. It seems that everybody in the place was in on the secret except for Mr. Scansaroli. Buck knew it. He wasn't involved in it particularly. But he heard it all going on. Kurek knew it, Natelli knew it. Scansaroli tells you "Oh, I didn't know anything about it." You are entitled to find that a false denial, and you are further entitled, if you believe it a false denial, to consider that false denial important proof that he was denying it because he knew it was criminal.

What about Mr. Natelli's credibility. Bear in mind your own impressions of Mr. Natelli when he testified on cross examination. The Government submits that you are

entitled to find from his demeanor on the stand that that man was incapable of giving a single straight-forward truthful answer. Ask yourselves how many times did he just wander off and have to be told what the question was again. Ask yourselves was he giving you a line of double talk. Ask yourselves was he telling you the truth. Because maybe you noticed and the Government submits that Mr. Natalli has a ~~mathematical~~ magical memory, a convenient memory. It's hazy on the things that tend to show his guilt and yet it's very firm and positive on the points he wants to make here, even after five years, and even when it is plainly inconsistent with documents prepared at the very time of the events in question such as Government's Exhibit 7, about the December 9 meeting, Government's Exhibit 16B the June 9 meeting, Government's Exhibit 14, about the June 3 meeting.

Mr. Natelli's testimony, in short, is just completely inconsistent with the rest of the proof. Ask yourselves if any other witnesses in the case behaved in this fashion. Ask yourselves did the defendants act as if they were telling the truth.

Look, there were conflicts in the proof. The defendants tell one story. The Government's proof, documentary proof in evidence, tells a completely different story. You are just going to have to decide this case by resolving

the conflicts in the proof. Use your common sense. Ask yourselves who has the biggest motive to fabricate, to hide, to cover up and deceive here. Just ask yourselves about that.

5b

Ask yourselves why the defendants' stories are utterly inconsistent with documentary proof. Documents don't change their story. Once they are prepared, there they are.

The Government contends in short that the defendants set about to bring the cover up right here into this courtroom, right there to the witness chair. The Government submits that they perjured themselves to cover up what it is that they did.

Again, if you find that they give false statements, you are entitled to find that they did so because they knew that they were guilty.

The Government submits, in short, that you can't believe these defendants. If you can't believe them, you must ~~convict~~ convict them.

Maybe you remember Mr. Stillman's opening. I do. He said something there. When I heard him say it, I said I wish I said that. Mr. Stillman told you the four hallmarks of a cover up which he calls a dirty word. It is a word nobody here invented. We need not to worry about personalities or lawyer's contests. He told you the four hallmarks of a cover up.

Number one, a scapegoat; number two, false statements, perjury; number three, missing documents; number

four, stonewalling. The Government submits we proved all of them.

Who is the scapegoat for the fact that all these contracts disappeared and turned out to be no good at all? Did these accountants own up to the fact that they did a lousy audit? Did they own up to the fact that they had no business booking this stuff for earnings of 1968? They find a scapegoat. Ron Michaels must have done something unethical. He absorbs all the blame for the fact that contracts had to be written off. That's a scapegoat. That's what they have here.

What about false statements and perjury? You have seen the documents in the case, the proxy statement. You are entitled to find that that's utterly false. They knew all of the things that we have proved here and didn't disclose. In fact, they doctored the books by subtracting the company's losses, National Student Marketing's losses, from other companies, false prepared statements.

What about perjury? That one is up to you. You saw the defendants testify. You are entitled to find, if you wish, that they have perjured themselves right here. What about missing documents? There is proof of that, too. There is a work paper for every single computation in this case except for that critical tax credit. As to that the defenda

are all over the lot. First there were papers, now there aren't papers. Mr. Natelli tells you there were papers and he's lost them, missing documents. There it is on a critical point.

The Government contends you will recall that that tax credit is a phony. Wouldn't it be interesting to find out what if any computations were done.

What about stonewalling? It is hard really to say what that term means. Ask yourselves if it means anything. Doesn't it mean the preparation of false documents? Doesn't it meanperjured statements? Doesn't it mean giving an explanation such as the tax credit? When the authorities begin to investigate, such as the SEC, there is no tax credit after all, it was really a mistake. Ask yourselves isn't that stonewalling? Ask yourselves if the Government hasn't proved all of these things?

I hopeyou will bear with me for just a minute or two more because I do want to show you what it is, help you if I can, in the work that you are going to have to undertake when you go to deliberate this afternoon.

The indictment charges two false statements. They are found in paragraph 3 and in paragraph 4 of count 2 of the indictment. You don'thave to memorize any of this. The indictment is going to be sent in to you. The exhibits

by the way, are going to be sent into you. If at any point you can't find a piece of paper you recall having seen, just send out a note. We are here to help you. If you need to find a piece of paper or where in the proxy statement certain things are or aren't, whatever, send out. You are entitled to ask for testimony, you are entitled to send for documents, you are entitled to all the help you feel you need.

The indictment in paragraph 3 focuses on the year ending 1968 and in particular to the footnote we have all been talking about. To sum up, it just tells you that the defendants knew that a million dollars of 1968 sales have been written off.

They knew it but they didn't tell anybody about it. In fact, they buried the loss by subtracting these losses from the pooled companies.

This chart summarizes it. A million dollars written off, nowhere disclosed, three quarters of a million dollars subtracted from the wrong place.

That's what that paragraph is about.

Ask yourselves as you decide with respect to that specification of fraud, they knew it, they didn't say it. They knew people were relying on it, too.

Paragraph 4 of the indictment charges a second

fraudulent financial statement. You are going to be instructed in a moment by Judge Tyler as to what the applicable law is.

I think it is fair to say that if you find the proxy statement false in either regard, you must convict.

The second regard has to do with the period ended May 1969. There the May figures showed $702,000 of earnings. Mr. Dingwall's calculations were that without these phony unbilled accounts receivables there were no earnings at all. The defendants knew it and didn't say it.

You have the Government charts which show what they knew about the two million being written off, the other ones they knew to be uncollectible. In addition, Paragraph 4 says that the sales were overstated by $800,000. That is summarized neatly for you right here in this chart. It shows when they found it out, where they wrote it down, totals it up for you, $800,000 of phony sales which they let go into those figures.

Now, these defendants are public accountants, certified public accountants. That means, as Mr. Natelli acknowledged on the stand, that the public is entitled to rely on them to give financial statements which are the truth.

The public is entitled to rely on financial statements which are truthful. That is the law. That is the law at issue in this case.

If you look at the proxy statement, Government Exhibit 25, you will see it is a beautiful thing. It is slick printing. Behind that slick printing job, fine layout, behind the cool forbidding certificate of Peat, Marwick, Mitchell & Company, one of the world's largest accounting firms, there are two defendants, Natelli and Scansaroli, right here, pushing the figures around, burying

losses in the pooled companies where they had no business doing it.

They knew that the company was a loser. They knew that the company was a fraud. They knew these things and they didn't tell anyone.

At the least, the very least, if accountants know that -- this isn't a technical matter -- if accountants know that the company is a can of worms like that, they have to say something. They can't just put out statements as they did here which show earnings and growth and sales which are utterly fictional.

Now, this is an important case. It is important for the defendants obviously, it is important for the Government to root out corruption and false statements and dishonest practices even when they occur in high places.

Reputation as we have all come to recognize recently is no defense when people have committed crimes.

I want to point up to one other thing about this case. Maybe you remember Mr.Frommer on the stand here, the man who used to have that company, Europe on Five Dollars a Day, put out the books, the travel company. Mr. Martin was cross-examining him. He said, Mr.Frommer, you could have hired accountants, couldn't you? You could have gone in and checked to see if National Student Marketing,

was okay or whether it was a loser.

Ask yourselves, isn't that a ~~simple~~ cynical question? Isn't that a question that says to you disregard the law, it doesn't matter that the law says accountants have to tell the truth. It is every man for himself, we don't need a law. Everybody will have to hire accountants from now on if they want to buy a share of stock or anything else in this country.

Well, we have a law. It protects Mr. Fommer and it protects you and me, and it says that accountants have to tell the truth in financial statements. That law isn't worth a hang, and all the prosecutors and judges and SEC lawyers and accountants, they aren't worth a hang if juries don't do their duty in a case like this one.

The Government leaves it up to you, up to your sense of duty, up to your common sense to stick with the issues in this case, to stick with the evidence, to decide this case according to your oaths, well and truly on the evidence.

We have all watched you as you sat here doing your work over what has been almost four weeks. It has been impressive. You have worked hard to pay attention to what sometimes must have been a little boring, sometimes has been technical or complicated. It is an important case.

We were all impressed with the hard work that you have done. Take your jobs seriously, as I am sure you will do. Don't feel overwhelmed. Jurors have sat in chairs like this one, like those for years since this building was built deciding cases just like this one. You don't have to memorize every item of proof, every number in this case. You are entitled to send for the exhibits or the testimony or ask questions of the Judge.

Use your common sense. Keep your eye on the ball. You shouldn't have any problem at all with this case.

You should also know that punishment which a defendant may receive in this court is absolutely none of your concern. Whether Judge Tyler decides to give them a suspended sentence or something else is absolutely on his conscience and has nothing to do with your concern at all.

I am going to ask you in doing your duty to set aside emotion, to set aside misplaced sympathy and focus on this evidence. Focus on the issues in this case. That is your duty, to do it. You have taken an oath. We are all going to trust you to hold to that oath.

Please bear in mind the overwhelming proof as to the motive here, documents whichshow it. Bear in mind the proof as to criminal intent, including the demeanor of

these defendants on the stand.

Bear in mind how the Government has shown that subtractions were made from pooled companies and there was absolutely no excuse for doing any such thing, showing an intent to deceive.

Abide by your oath, abide by your common sense, stick with the evidence.

And the Government is confident you will find these defendants guilty as charged.

Thank you.

THE COURT: Ladies and gentlemen, we will take a morning recess at this point. It will be about ten minutes.

(Recess.)

CHARGE OF THE COURT

(Tyler,D.J.)

THE COURT: Mr. Light and ladies and gentlemen of the jury:

As you approach the highly important task of citizenship of deliberating in this case, please remember that it is your duty to weigh the evidence calmly and dispassionately, without sympathy or prejudice for or against either the Government or the two defendants here on trial.

As I think all of you understand, our system of jurisprudence defines the duties of the Judge on the one hand and the duties of the jury on the other. It is exclusively the function of the Judge to set forth the rules which govern the case with instructions as to their application.

On these legal matters you must take the law as I give it to you in the next moments and you will not concern yourselves with statements as to the law which counsel may have made during the course of their summations or at any other point during the trial.

For what I am sure are perfectly obvious reasons, you should not single out any one of my instructions

as alone stating the law, but you should consider my instructions as a whole when you retire to deliberate in the jury room.

I want to make it very plain at this point that my actions during this trial in passing upon motions or applications made by counsel or in overruling or sustaining objections made by counsel are not to be taken by you as any indication of the guilt or innocence of the defendants.

As I am sure you understand, counsel not only have the right, but indeed they have the duty to object to the introduction into evidence of any statements or exhibits or testimony which they believe should not be admitted. These are questions of law and procedure with which you should have no concern when you retire to deliberate.

I ask you to draw no inferences from the fact that upon occasion I asked questions of certain witnesses. For better or for worse, these were only intended for clarification or to expedite matters and certainly were not intended to suggest any opinions on my part as to the guilt or innocence of either of the men on trial or whether one of the witnesses who appeared in our case before us may have been more credible than another witness.

I want to emphasize to you once again that it is your recollection and your understanding of the

evidence which came out here in your presence in this room during our trial and only your recollection and your understanding of that evidence which can serve as a basis for your findings in this case.

This proposition flows from the basic principle that you the jury must keep in mind at all times, that is, that you are the sole and exclusive finders and judges of the facts based upon your recollection of the evidence.

Therefore, if I should state in my remarks any evidence as I recall it, please keep in mind that I do not intend to state the evidence is truly such or that a particular witness actually did testify such and such. My only point will be to illustrate some principle of law which I am discussing.

To sum this point up, ladies and gentlemen, any statements which the lawyers or the Judge may have made about evidence in the case which does not accord with your recollection of that evidence, you should put aside what the lawyers and Judge said and accept your recollection as controlling.

End7A

The law presumes a defendant such as Anthony Natelli and Joseph Scansaroli to be innocent of charges of crime. As I told you at the outset, and I repeat here, the indictment in this case is merely an accusation or a charge. It is no evidence or proof of a given defendant's guilt and it does not detract one whit from the presumption of innocence in favor of a given defendant.

You will not give any weight whatsoever to the fact that a grand jury in this building returned this indictment, including this particular charge known as Count 2 therein, against these two men as any evidence of guilt on their part.

As you know, prior to our trial each defendant pleaded not guilty to count 2. Thus, as Government counsel knows, the Government has the burden of proving the charges against the defendants beyond a reasonable doubt. It is a burdant which never shifts and remains upon the prosecution throughout the trial.

Under our system a defendant does not have to prove his innocence. On the contrary, as I have stated, he is presumed innocent of the accusations contained in count 2 of this indictment. This presumption of innocence was in favor of each of the two defendants at the start of the trial, it has continued in their favor throughout the trial,

it is in their favor as I speak at this moment, and it remains in their favor during the course of your deliberations in the jury room.

It is removed only if and when you are satisfied that the Government has sustained its burden of proving the guilt of a given defendant beyond a reasonable doubt.

The question that naturally comes up at this point is what does the law mean by this concept or rule of reasonable doubt.

In a sense you could say that the words come close to defining themselves. Reasonable doubt is a doubt founded in reason and arising out of the evidence in the case or perhaps from lack of evidence. It is a doubt which a reasonable person has after carefully weighing all of the evidence. It means a doubt that is substantial and not just shadowy or ephermeral. A reasonable doubt is one which appeals to your reason, your judgment, your common sense and your experience in life.

It is not caprice, whim or speculation. It is not an excuse to avoid the performance of a difficult or unpleasant duty. It is not sympathy for the defendants.

Rather, ladies and gentlemen, the law succinctly defines a reasonable doubt to be a doubt which would cause prudent persons to hesitate before acting in matters of

importance to themselves.

Finally, of course, on this subject I point out that a reasonable doubt does not mean beyond all possible doubt. If the latter were the applicable standard, few if any men and women would ever be convicted of any criminal accusation.

As you and I know, it is practically impossible for a human being to be absolutely convinced of any controverted fact which by its nature is not susceptible of mathematical computation.

Now, during this trial I think the lawyers and I trust the judge have stressed to you that the case is to be decided only on evidence admitted in your presence in this courtroom. It is understood under our system that there are two general types of evidence.

One is called circumstantial evidence, about which I will say some more in a moment, the other is called direct evidence. Examples of the latter are testimony of witnesses who appeared here in this chair on my immediate right and were sworn and gave evidence on direct and cross examination.

Another form of direct evidence, of course, would be pieces of paper or physical objects which were admitted into evidence in your presence. Still another form of direct evidence, so-called, would be stipulations of fact which you

recall were entered into by the lawyers on behalf of their respective clients.

This is all of the direct evidence, and the only direct evidence which you are to consider in your deliberations. Any evidence as to which an objection was sustained by the Court, as you know, you should entirely disregard.

Questions asked by the lawyers or questions asked by the Judge, of course, in themselves are not evidence. It is only the answers of the witnesses taken in light, of course, of the questions they are answering which are evidence.

Of course, as I have stated, the opening and closing arguments of counsel to you are not evidence.

Incidentally, regarding stipulations of facts entered into by the lawyers, you should consider each stipulation which you recall only in regard to the defendant or defendants who joined in or agreed to such stipulation.

Now, in addition to your consideration of the direct evidence, so-called, you are permitted to and indeed you should consider what is called circumstantial evidence.

Whether you are considering direct evidence or circumstantial evidence, you must accept and apply in your deliberations thereon, any presumptions or other rules such as the presumption of innocence and the rule of reasonable doubt about which I instructed you a moment ago.

Now, you have heard examples given to you here in

this trial of circumstantial evidence. You yourselves, I'm sure, have dealt with the concept of circumstantial evidence in your own lives.

Very simply, for our purposes, I will define circumstantial evidence as evidence which does not itself directly establish a fact sought to be proved, but instead may lead you to the fact sought to be proved by the every-day process of reasoning or, as it is sometimes called, inference or inferences to be drawn from direct evidence in the case.

Now, you remember that at the outset of this trial it was pointed out to you that the only count in which the defendants here on trial, Messrs Natelli and Scansaroli, are named, is count two of the indictment.

I read that count to you in significant part at the start of this trial about four weeks ago. I read it to you in significant part once again.

However, as has been pointed out correctly to you by counsel, you will have a copy of this count as a guide in your deliberations, and the clerk and I will see to it that it is given to Mr. Lights, your foreman, on your behalf to use as such a guide.

Let me read it to you again.

"The grand jury further charges:

"1. On or about September 27,1969," in this judicial district, "defendants Cortes Randall, Robert Bushnell Dennis Kelly andBernard Kurek, as responsible officers of NSMC, and Anthony Natelli and Joseph Scansaroli, as independent auditors of NSMC, unlawfully, wilfully and knowingly made and caused to be made false and misleading statements withrespect to material facts as set forth in Paragraphs 3 and 4 of this count in a proxy statement for NSMC, dated September 27, 1969.

"2. Said proxy statement solicited approval by the NSMC shareholders of the issuance of additional shares of NSMC common stock and the approval of certain mergers, and was required to be filed and was filed with theSEC" -- andyou understand parenthetically SEC stands for theSecurities andExchange Commission of the United States of America -- "pursuant to Title 15, United States Code," and thenit gives certain sections thereunder which, in fact, are certain sections of the 1934 Securities Exchange Act.

"3. Said proxy statement contained an audited statement of earnings for NSMC for the fiscal year ending August 31, 1968, which differed from a previous audited statement of earnings for the same period contained in an

annual report to stockholders for that fiscal year. The difference was explained in the following footnote," and then there is quoted the footnote which appears in that proxy statement, ladies and gentlemen, which, as you know, is in evidence as Government Exhibit 25.

The footnote which is quoted here is to be found on Page 23 of that document, Government Exhibit 5, and it is listed on that page as Footnote D.

And then, furthermore, the indictment language goes on to recite not only that footnote in terms of substantive language, but certain columns of figures which I will not repeat here except to summarize to say that they are figures for the year ending August 31, 1968, and they have to do with net sales, so-called, and net earnings, with various subdivisions thereof as recited on Page 23 of Government Exhibit 25.

Continuing my reading of Paragraph 3 of Count 2, I quote:

"This explanatory note was materially false and misleading in the light of the circumstances under which it was made because, as the defendants well knew but failed to disclose, among other things: (a), approximately $1 million, or more than 20 per cent of the 1968 net sales originally reported had proven to be non-existent by the

time the proxy statement was filed and had been written off on NSMC's own internal books of account; (b), net sales and profits of 'pooled companies reflected retroactively' were substantially understated; and (c), net sales and profits of NSMC were substantially overstated."

Finally in Paragraph 4 of this count it is alleged as follows:

"Said proxy statement also contained an unaudited statement of earnings for the nine months ended May 31, 1969, which stated net sales as $11,313,569 and net earnings as $702,270. These figures were materially false and misleading because, as the defendants well knew at the time the proxy statement was filed, net sales for that period were less than $10,500,000 and NSMC had no earnings at all."

Incidentally, according to my recollection and understanding of the evidence, the figures which are quoted and set forth in Paragraph 4 of Count 2 appear at Page 21 of Government Exhibit 25 in evidence under the Column 1969.

Therefore, having read the indictment, and as you understand, Count 2 charges the two defendants, Natelli and Scansaroli, with criminal responsibility for certain financial statements contained in the proxy statement which was dated the end of September 1969 and said statements are said to be false and misleading in a material sense and, of course, were part of the proxy statement which was filed with the SEC.

In considering this charge I emphasize to you that you must consider the guilt or innocence of each of these two men separately. This means, among other things, the point that you should reflect upon the evidence as it pertains to and affects each of these men separately. As you can well understand, the criminal law regards guilt or criminal culpability as a personal thing.

You also know in this connection, of course, that the two men on trial were certified public accountants employed by the same firm, and not only that, by the same office thereof, that is, the Washington, D. C. office.

You know also that they worked together. I think you could infer from their own evidence here that they not only were associates in work, but they were friends.

Mere association, of course, is no proof of any guilty conduct whatsoever -- you understand that -- and the Government would not contend otherwise. Therefore, it is important to remember that you have got to consider the evidence as it bears upon and pertains to these two men separately.

By way of background here I want to discuss with you the law or laws which are alleged to be violated in Count 2. A reference has already been made to the Securities and Exchange Commission and throughout the trial, as you know, and indeed in my remarks that Commission will be referred to as the SEC.

I think many of you know that the SEC is an agency of the United States Government. It was created by the Securities Exchange Act of 1934, that is to say, passed by the Congress in that year.

Generally speaking, the laws administered by the Commission relate to the field of securities, the issuance and sale thereof, and they seek to provide protection for the public in securities transactions. The 1934 Act, portions of which are alleged to be violated here

in Count 2, together with the rules promulgated by the SEC thereunder generally provide that a company which has filed a registration statement with the SEC must thereafter file with the SEC such other documents as the rules of that agency prescribe.

I do not think there is any dispute but that NSMC was at all times here relevant a registered company, that is to say, that they had filed a registration statement before the events here began to unfold with theSEC.

The SEC, among other things, in the times relevant here, required that all proxy statements of registered companies must be filed with it, that is to say, the SEC. Therefore, it was with those requirements in mind -- and again, I don't think there is any serious dispute about this -- that the officers and management of NSMC in the summer and fall of 1969 were getting together a proxy statement to file with the Commission because they intended to either merge with or acquire I think it is four other companies, and in the bargain, they were going to have additional shares of stock be issued by the company because shares of stock in whole or in part were going to be exchanged in these acquisitions or mergers.

Now, as you probably glean, the purpose of the

requirement of filing of information such as a proxy statement is, generally speaking, to have on file, available for public scrutiny or to be scrutinized by those members of the public who care to look, information about the issuer of securities, meaning by that a company issuing its own stock, which is current and up to date and as reasonably accurate in all material respects as possible.

Now, there is a provision in the 1934 Act which reads in relevant part for the purposes of count 2, that is to say, our case, as follows:

"Any person who wilfully and knowingly makes or causes to be made any statement in any document required to be filed under this title or any rule or regulation thereunder, which statement was false and misleading with respect to any material fact, is guilty of a crime."

As I have already stated or at the very least inferred, count 2 is laid basically upon this statutory language which I just read to you.

In practical, simplistic terms, therefore, count 2 charges the defendants with preparing and filing a false and misleading proxy statement in material respects, in violation of the law.

Now, you also I think already understand that count 2 charges that the proxy statement as a whole was not false but that it was false and misleading in two material respects.

First, count 2 charges that the defendants omitted or caused to be omitted disclosure that over $1 mill worth of NSMC's 1968 gross sales had been written off and that the defendants had subtracted in the proxy statement figures the greater part of the losses not from the gross

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revenues of NSMC but from the gross revenues and earnings of the so-called pooled companies, that is to say, companies which had been acquired by NSMC before the proxy was filed, thus overstating NSMC's sales and earnings and understating the earnings and sales of the pooled companies.

Second, count 2 charges that the defendants either overstated or caused to be overstated in the proxy statement NSMC sales and earnings for the first nine months of 1969, omitting to disclose that NSMC had no substantial earnings at all during that nine-month period.

Now, I instruct you that if you find that the proxy statement was false in either one of these two respects that is sufficient to support a conviction. Put differently the Government isn't required in order to support a conviction here to prove that both parts or both false and misleading statements, so called, of material facts were such in order to support a conviction.

As the lawyers have all fairly pointed out to you, we have heard a great deal of evidence, there has been a considerable volume of evidence, particularly documentary evidence, in this case. In a sense or in various senses, it could be truly said, as I think the lawyers have, that some of this seems to be complicated. However, it could be said that generally speaking the issue which you

really have to focus on here can be stated in a relatively simple fashion: Did the defendants or either one of them knowingly and intentionally either prepare and submit material misstatements as to the financial position or financial operations for NSMC for the year of 1968, for which the figures were stated to be audited, or in respect to the figures for NSMC for the first nine months of 1969, which were, as I recall the proxy statement, labeled as unaudited figures.

If you were to determine that in neither one of the two respects alleged the statements were false or misleading, why, then, of course, you would be obliged to acquit both defendants.

On the other hand, if you were to determine that in either or both respects the financial information or data or figures were in fact false and misleading in a material sense, then you would be obliged to consider whether or not the defendants knowingly participated in making these figures and putting them in the proxy statement to be filed with the SEC, and if you did find that they either knowingly made these misstatements or they caused them to be made or they aided and abetted in their making, then you would be obliged to convict the defendant or defendants for which you make these findings.

Now, before I turn to the elements of the offense which the Government must prove beyond a reasonable doubt and then discuss with you the principles of law to be applied to those elements, it might be helpful to you in your deliberations if I were to summarize some of the main contentions of the parties here, then turn to the elements and instructions of law, with the hope that my summation of these contentions will illustrate the principles of law which I will treat and define and explain to you.

Now, I have set forth and read to you the accusations in the indictment. As you know, both Scansaroli and Natelli deny by their pleas of not guilty their culpability as alleged. More specifically than that, for example, Scansaroli argues that all of his work as a supervisor on the NSMC engagement was work performed by him to the best of his professional ability as a certified public accountant and in good faith.

He argues that the footnote to the 1968 financials in the proxy statement, so far as he knew, was a sufficient disclosure and that there is no showing beyond a reasonable doubt that there were material misstatements made to the SEC as to the company sales for the unaudited period ending May 31, 1969.

He argues that the testimony of Natelli alone shows that all of the significant and material decisions at issue in this case were made by Natelli as the partner in charge of this particular engagement and that the decision with respect to the footnote disclosure was discussed and approved by the senior partner of PMM, Mr. Leon Otkiss, in the Philadelphia office.

Scansaroli contends that he used good judgment or the best and honest judgment that he could make in his role as supervisor in respect to the 1968 audit. He simi-

larly makes the same claim with regard to confirmations which he did of that audit. He says that everything he did was done, so far as he knows, in an honest attempt to comply with reasonably understood accounting practices i that particular profession.

He also would call your attention to the testimony of the witness Berman who, as I recall it at least, was not able to identify Scansaroli as the gentleman he visited over in the offices of Peat, Marwick and Mitchell in Washington.

Indeed, I believe, as I recall it, not even Scansaroli could identify Berman in the flesh as he appeared here.

However, Scansaroli asked you to consider, and certainly you may if you would like to, that Berman's evidence is important for two reasons.

One, it could only have been Scansaroli to whom Berman was referred because he was the supervisor on that particular NSMC account at the time and, two, Scansaroli was doing most of the work at that time at least in regard to the figures and, therefore, Berman, who told us he didn't seem to get any refusals or hesitations on the part of Scansaroli to show him any work papers or answer any questions, this is proof that Scansaroli was proceeding in good faith as an honest accountant at the time.

Scansaroli also contends that his review of some of these fixed fee contracts in May 1969 is evidence of his good faith in an attempt to comply with reasonable accounting procedures in evaluating these accounts which were so important to NSMC at the time.

He also argues that he's the man who saw to it that Douglas Oberlander, a somewhat more junior accountant at PMM, did another review of these so-called accounts receivable or fixed fee contracts, as they have been interchangeably referred to in our case. And, says Scansaroli, how would he have put a digger like Oberlander on the job if he was trying to engage in some kind of criminal cover up or something of that nature.

Scansaroli also argues that his lawyer withdrew from witnesses Johnston and Oberlander and perhaps others when they testified here, that so far as they knew, he, Scansaroli, never asked them to do anything specific which amounted to something criminal or in the nature of a cover up of the financial data and affairs of NSMC.

Scansaroli also points to the testimony of Natelli, which he says and argues to you he believes to be truthful and correct, and he also argues to you shows that he Scansaroli, couldn't have been culpable because he was only doing what Natelli told him to do, in any event, under the

layer of responsibilities which PMM had set up for its various employees in this type of an engagement.

Scansaroli also argues that he did not only an honest and a good job on trying to confirm a lot of these accounts receivable, but that any problems that arose therefrom were all due to the fact that there was a dishonest account executive in thisfirm known as Ron or Ronald Michaels and that it was the Ron Michaels dishonesty in claiming a lot of contracts or accounts which turned out to be phony or false that created all these problems, and that once that came out into the open, everything that he, Scansaroli, did was significantly honest and as good a job as he was capable of doing at the time.

In sum, as you well know, Scansaroli contends that he is innocent of any concealment or any assistance in or causing any material statements to be made which were false and misleading inthe proxy statement in either regard as alleged in count two of this indictment.

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As you well know, although the defendant Anthony Natelli had a very different role perhaps in accounting terminology and practice at least, he similarly makes contentions very much like those of Scansaroli.

He has pleaded not guilty also to this charge. More particularly in the context of his role as the supervising partner of the Washington office and the supervising partner of the NSMC engarement, he states a number of arguments, which I will try to summarize in significant part, although not totally, for you.

Natelli points out that his office was retained as the outside auditor for NSMC very late in the summer of 1968, virtually at the completion of the fiscal year at that time of that company. As you know, at that time at least, in 1968, the fiscal year of this company ended on August 31 of the year.

Natelli pointed out that they came in, they succeeded Arthur Andersen, and that he was aware that they were going to have to get down to work and perhaps deal with some problems of record keeping because of earlier practices by NSMC; that he, Natelli, made an honest, professional judgment in the weeks and few months shortly thereafter to change the method of accounting to what has

been called here by various witnesses the percentage of completion method of accounting; that he strove to put together a team of accountants from his office under the supervision of Scansaroli to get at the job; and that they did a good, honest job to pick up, and try to check back as to what was done.

Natelli also points out that he was aware that NSMC at the time was a young but rapidly growing concern where perhaps recordkeeping and financial accounting procedures had not theretofore been done as well as might have been done.

He contends that recognizing these circumstances he and his staff did the best, honest job they could to cope with the situation in a professional way.

Natelli argues that he was instrumental, among others at least, in trying to get the NSMC management to verify the existence of some of these contracts. He says that he had Kurek himself prepare a list of the contracts and he then instructed Scansaroli to discuss these contracts up here in New York City with the account executives or salesmen.

Indeed, Natelli says it was he who instructed Scansaroli to confirm, as accountants use that word, these accounts receivable.

You know from the evidence or at least I recall the evidence which was given in this case, that Scansaroli came to New York and did, in fact, talk to these account executives and then he made a variety of phone calls. You remember all of that.

Now, Natelli also argues to you that after Scansaroli returned from this job in New York, that he, Natelli, decided at that point finally that the percentage of completion method was a fair and viable method of accounting, to fairly reflect and honestly reflect NSMC's financial position at the end of any accounting or auditing period or at any other time.

Natelli argues to you that not even the Government contends that in the fall of 1968 the work of the PMM team under the leadership of Natelli was criminal. Natelli argues that they did the best they could under a somewhat difficult situation and that they tried to pull together the 1968 figures and audited them as any decent professional accountant would do.

As a matter of fact, Natelli points to a December meeting about which you have heard much from various witnesses isn this case and says that at that meeting he, Natelli, was leading and insisting that the NSMC management come up with better records for the future, including

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written, that is to say, not oral commitments for these contracts which are the subject of this case.

Turning to the writeoffs about which there is considerable evidence, Natelli makes a number of arguments. For example, he argues that the company management itself wrote off certain of these contracts. As to the others which were written off at the instance of PMM, Natelli like Scansaroli says that these devolve from the somewhat unique and unusual situation of employee misconduct and fraud; that is to say, the behavior or activities of Ron Michaels.

Natelli argues that once he had learned that Michaels had been fired and that the commitments that Michaels had reported never existed, he then himself concluded that the Michaels contracts should be written off as of August 31, 1968, and that this was an honest, prudent, professional judgment on his part.

Getting down to the proxy statement, Natelli has testified and he argues that he had no intent to deceive or mislead anybody, although he admits that he had considerable personal direct involvement in preparing particularly the drafts and redrafts of the footnotes, including the footnote which is set forth verbatim in Count 2.

Natelli did say, however, as I recall it, that

he did not have responsibility for bringing in the figures. That responsibility, lay, as I understood him, with Scansaroli and perhaps other accountants on the NSMC team put together by Peat, Marwick & Mitchell.

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But in any event, Natelli says that there was no intention on his part to omit any needed disclosures nor was there any intent on his part to misstate or mislead as he did his drafting and redrafting.

Moreover, Natelli claims that when the write-offs were made and certain other matters were brought into play, such as the tax deferred item or the tax credit item, that it boiled down to such a small net difference that it was relatively unimportant and immaterial for recording purposes in any event.

Now, turning to the so-called comfort letter, which this Court permitted to come into the evidence in this case even though, as you well know, the comfort letter was not submitted or really even prepared in draft until late October, which was well after the preparation of the proxy statement.

Natelli points to the fact that he was home ill or -- I am not sure I understood it, whether he was ill or whether he was home because he had to go for some medical checkup -- but he was home on Friday, October 31, and that he received calls from people like Johnston and Colona in which they were very upset about certain of these writeoffs, certain of these contracts which hadn't been written off, and according to Natelli, he treated that in the only honest way possible.

He referred Colona to Leon Otkiss. Though it was late in the day, he suggested that Otkiss be called in the morning.

I think I have my dates incorrect here. I think this was on the 30th. It was on the next morning that he suggested to Colona that he call and that Colona in fact called and that thereafter Natelli, who came back to the office that day, had a number of conversations that morning with Otkiss, and that he presented the problem fairly and completely to Otkiss and that Otkiss agreed with him, but Otkiss suggested that maybe they ought to consult with Mr. Holton, a still more senior partner here in New York, the chairman of PMM's practices committee, and in fact they had a conference call, and you remember that Otkiss told us about that and Holton told us about that as well as Mr. Natelli, and we thereafter heard from counsel for PMM, who told us he was very concerned with certain of the information and what he did and tried to do and all that.

Now, Natelli says also that at the closing which took place in the office of White & Case here in New York in the late afternoon of Friday, October 31, Natelli, as I recall his evidence, said that he was pointing out to NSMC and the lawyers that they might better have to go to the SEC about the problems of some of these writeoffs and account receivable and so on, and therefore Natelli argues to you, "Look, if I were a guilty man I wouldn't be telling anybody

we might have to go to the SEC about all this because that would mean that the SEC would look into it and would catch me, among other guilty parties, if there were any."

Therefore, the comfort letter and the events surrounding it are argued by Natelli to show that he was proceeding with utmost good faith and that he wouldn't ever dare bring this to anybody's attention, including even his own people at Peat, Marwick, if he were guilty of any coverup or wilful and knowing false misstatements of material facts in the proxy statement.

Well, the Government, of course, has quite different contentions. The Government's first contention, in point of time, at least, is that in the months and weeks following their retainer, that is, PMM retainer, in August 1968 Natelli and Scansaroli were extremely lax and negligent in permitting their client to add about 1.6 or $7 million worth of sales to the results for the fiscal year ending August 31, 1968.

The Government points to the testimony of Kurek, Buck, Oberlander, Johnston and others, and to the exhibits in evidence, to show, as the Government sees it, that these sales first really surfaced so far as Natelli and Scansaroli were concerned in mid-October, that the two men quickly learned or should have learned that they

were not legally binding commitments, and that the salesmen on these alleged sales weren't even entitled to commissions, and that the whole picture was one where any accountant of even a minor amount of experience should have known that the contracts were very, very questionable indeed, particularly to the extent of showing a great amount of income on audited returns for a fiscal year.

The Government then goes on to say that the total picture, most particularly the documentary evidence, the work sheets and the like of Peat, Marwick, Mitchell, shows that this was a lax, careless, unprofessional job of auditing and that as time went on, though it was true that occasionally Natelli and Scansaroli and others would remonstrate about getting written commitments, they got deeper and deeper into trouble because they were lax in their auditing work, and they were particularly lax in clamping down on the management people who were involved in struggling to get these commitments on the books so as to present a rosey financial picture to putative merger partners or companies which might be acquired or bought by NSMC.

The Government points, for example, in this period, to the so-called confirmation procedures, which were oral and telephonic, and the Government argues that they were about as absurd and unprofessional and as poorly

designed to get at the true facts as anything that could be conceived, particularly by certified public accountants.

The Government argues that the trip of Scansaroli to New York was as futile a venture and trip as could be imagined, that he took the word of these account executives, that he made calls to people that he didn't even know, and that he got information which at best was inconclusive, assuming it came from persons who really knew what they were talking about in any event.

Therefore, the Government says that what went on in the fall of 1968 in connection with the audit of the '68 fiscal year figures was so lax and so careless and so inconclusive, particularly in respect to these important sources of income, the fixed fee contracts, that it was a very poor job and that what happened in 1969 was almost inevitable to the knowledge of any responsible accountant, that is to say, when they came to the point where they started making writeoffs.

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Now, the Government, as you know, makes the argument here that after the '68 audit was complete, in a very few months, to the knowledge of Natelli and Scansaroli, both NSMC management and, when the Michaels situations at least came along, Natelli and Scansaroli themselves were writing off almost $1 million worth of these receivables for the year 1968 as no good, that is to say, as uncollectible accounts receivable.

The Government argues that during this period at the very latest Scansaroli and Natelli began to be aware that they werein very deep and that their professional lives might be at stake and they began to express concern to various figures in management at NSMC and there were meetings held and conversations over the telephone.

As an illustration of this, you know it has been much bruted about by all counsel in the case, certain documents would show that Scansaroli, at least, expressed concern about losing his license. There has been testimony from Kurek on this subject.

Scansaroli and Natelli say that this never happened at all, or more precisely, as I understand them, they say, well, one or the other of them might have said jokingly that they might lose their license, but it was just a joke and that was it.

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into the figures, as the Government would have it, in place of Pontiac.

Now, the Government argues that nobody, nobody, least of all Scansaroli and Natelli, had ever heard of the Eastern Airlines commitment until the wee hours of mid-August when they were here at Pandick Press, and the Government says that from everything that these two defendants knew about the write offs up to that point, they should have been very skeptical if not downright suspicious about the commitment, but, says the Government, from their evidence they proved from the lips of Mr. Buck, for example, that Natelli didn't bat an eye and in went the Eastern figures.

Therefore, the Government argues that they have shown that at that time Natelli well knew that this was all bogus material and that these entries as alleged in count 2 were woefully misleading in that they made no disclosure of the write offs at all, and worse than that, the write offs were concealed by having them subtracted from the pooled companies revenues and not from the revenues of NSMC, which in very simple terms resulted in the figures showing a profit for 1968 and 1969 for NSMC whereas in fact in 1968 there should have been a loss and in 1969 no appreciable net income at all.

Finally, the Government says with respect to the

comfort letter "sure, we will concede that Natelli talked to Otkiss, that Natelli talked to Holton, and we will even concede that at one point or another in October Natelli may have said to Randall and others. Look, we have got to straighten this out in connection with this closing or we may have to go to the SEC," that is to say, they might have to file amended figures with the SEC, and the Government says, "Look, all that was, Natelli knew full well that he and Scansaroli were then in it and that this was designed to throw everybody off the track. Not only the SEC," says the Government, "but Mr. Otkiss and Mr. Holton."

The Government argues, in other words, that Natelli didn't really bring all of the facts and the true facts to Otkiss' attention when he consulted him by phone.

Well, I don't intend to go on and I don't want you to ignore the fact, and it is the fact, that I haven't summarized every argument that able counsel have made for their clients, and I don't intend to. I have hit what I understand to be the high points and these points have been argued early and often by able counsel for each of the defendants and for the United States.

My point is to set a back drop for us because I now intend to turn and discuss with you the essential elements of this offense which the United States must prove beyond a

reasonable doubt to support a conviction of either or both of the defendants.

The first essential element is that NSMC filed a proxy statement with the SEC which was required by law so to be filed.

Now, I don't understand that there is any significant issue about this element at all. I don't think that you need, therefore, to waste much time on that, which is virtually, as I understand it, conceded.

The second essential element is as follows: The Government must prove beyond that one or both of the matter or statements made in the proxy statement was false or misleading and materially so. Put differently, that the statements were false or misleading as to a material fact or facts.

The third essential element which the Government must prove beyond a reasonable doubt is that the defendant in question either made or caused to be made the false or misleading statements or one of them.

Fourth, you must be satisfied beyond a reasonable doubt that the defendant in question acted wilfully and knowingly.

I am going to discuss some of the principles of law involved in these essential elements so called and your consideration of these essential elements.

The term or phrase "false and misleading statement" has been discussed. I point out to you that under the law a statement is false, of course, if it is untrue. A statement is misleading if it omits facts which are necessary to portray a true picture of the facts which are relevant. A statement is false or misleading if what is stated conceals or distorts a material fact so that the omission or failure to disclose creates or fosters a misapprehension as to the true state of facts which are relevant.

In this context keep in mind that sometimes a half truth is no better than an outright falsehood. A misleading effect may be created by half truths.

Indeed, a statement, though literally true, can nevertheless be false if it would create a false impression of the true state of affairs when interpreted by those who would read the statement in question.

Now, where a person represents that a particular fact or set of facts exists, but at the same time willfully and knowingly and intentionally fails to reveal other relevant and material facts concerning those representations which are made, and thus would place the state of affairs

in quite a different posture if these additional facts were known, he may have an obligation to disclose these other material facts so as to avoid deceiving persons who read the statement or statements in question.

To illustrate here, as you know, the Government argues that in respect to the celebrated footnote D, about which you heard so much here, . to the extent that that footnote receites that NSMC's 1968 sales were 4.9 million, it does not disclose that NSMC had written off about a million dollars worth of these sales. Therefore, the Government would say that though part of this is the truth, it is only a half truth and, therefore, it is misleading and false.

Now, on the other side of the coin, as you know, the defendants both argue that this is substantially correct and isn't material in any event, because of other figures and therefore, it isn't false and misleading as the law understands those terms at all.

In the context of this case I instruct you that a defendant may be found to have acted wilfully and knowingly only if he knew that a portion of the financial statements recited in count 2, such as the footnote or a figure entry, was false and misleading. It is not enough, in other words, merely to establish that a given defendant acted negligently

or through error or mistake. Although mistakes or negligence may give rise to civil suits, they do not constitute criminal conduct.

A finding of an intention to include false and misleading information of a material nature is required. Good faith, that is to say, an honest belief in the truth of the data set forth in the footnote and entries in the proxy statement, would constitute a complete defense here.

I point out that the prosecution, however, is not required to prove the making of the alleged false or misleading data or the defendants knowing, intentionally participations therein by direct proof, that is to say, by direct eyewitness evidence or the like. These elements of knowledge and intent, in other words, may be proved by circumstantial evidence, that is to say, by such inferences as may naturally and reasonably be drawn from all of the facts and circumstances as shown by the evidence in the case.

While I have stated that negligence or mistake does not constitute guilty knowledge or intent, nevertheless, ladies and gentlemen, you are entitled to consider in determining whether a defendant acted with such intent if he deliberately closed his eyes to the obvious or to the facts that certainly would be observed or ascertained in the course of his accounting work or whether he recklessly stated as

facts matters of which he knew he was ignorant.

If you find such reckless deliberate indifference to or disregard for truth or falsity on the part of a given defendant, the law entitles you to infer therefrom that that defendant wilfully and knowingly filed or caused to be filed false financial information of a material nature with the SEC.

But such an inference, of course, must depend upon the weight and credibility extended to the evidence of reckless and indifferent, conduct, if any.

I repeat: Ordinary or simple negligence or mistake alone would be insufficient to support a finding of guilty knowledge or wilfulness or intent.

Now, in this connection one circumstance you are certainly entitled to consider and weigh in determining whether one of the defendants acted wilfully and knowingly is whether he as an accountant followed or deviated from generally accepted auditing or accounting standards in effect at the times here pertinent.

For example, in this case you may recall evidence of certain accounting principles or standards which were talked about and, indeed, in part read into evidence. One of them you may remember is so-called APB No. 9.

Now, both defendants, as you know, contended that they acted honestly and in good faith, in accordance with generally accepted auditing and accounting standards in vogue in 1968 and 1969.

Conversely, the Government points to evidence from witnesses which they say establishes that both Scansaroli and Natelli deviated from sound accounting principles. Evidence on either side of this issue is not conclusive, however, on the overriding issue of the defendants' knowledge and intent.

Thus, the fact that a given defendant's conduct was in accord with such standards and principles does not necessarily or automatically constitute a complete defense to this charge.

The weight and credibility to be extended by you to such proof must depend, among other things, on how authoritative you find the precedents and teachings relied upon the parties or the extent to which they contemplate or deal with the circumstances found in the documents in evidence here and on the weight you give to expert opinion evidence offered by various witnesses.

Conversely, evidence that a defendant's conduct was not in accord with sound accounting standards does not automatically or necessarily mean that that defendant

is guilty of this charge.

As has been already stated to you, these considerations are relevant and would bear one way or another on guilt or innocence even though they are not absolutely and automatically controlling.

Generally, as you have been told, in effect, a firm of public accountants, such as Peat, Marwick & Mitchell, engaged to perform an independent audit for a corporation such as NSMC, represents and warrants that it will perform the audit and other accounting work in accordance with generally accepted auditing and accounting principles, that it will render an opinion based upon its audit, for example, as to whether the financial statement of the company fairly presents its financial position and the results of its business operation.

Proof that a defendant departed from such standards of auditing and accounting or participated in the preparation or approval of a financial statement that did not fairly present NSMC's financial position is evidence not necessarily conclusive that that defendant did not act honestly, in good faith, and that the statements contrary to such standards may have been materially false or misleading.

On the other hand, proof that the defendant in

question did act in accordance with generally accepted auditing standards is evidence which you may find persuasive but not necessarily conclusive that he acted in good faith and that the facts as certified by him or made by him were not materially false or misleading.

Now, I have been talking about material facts. You heard material facts being discussed by lawyers and witnesses during the trial. I want to define here for you what thelaw means about material facts.

Let me approach it for you in this way. In deciding whether a fact is material, ladies and gentlemen of the jury, you are entitled to consider whether it was the kind of information that a financial statement ordinarily contains in order to fulfill its function of fairly presenting the financial picture of the company for which it is filed.

A material fact can be simply defined as one that would matter to a reasonable person in deciding whether or not to purchase NSMC's stock, for example. That is to say, a fact, the validity of which would concern a reasonable person in making his purchase or investment decision.

Obviously a balance sheet or income statement is not supposed to contain all the information a creditor or potential investor or stockholder might need or want to

know in order to make informed judgments. The function of the financial statement is simply to present a basic summary of the company's financial position and operations and earnings for the time period stated.

Now, in this connection I point out to you, and I should have made this point earlier, but I think you understand it, no one is contending, and it certainly is not the fact, that an outside auditing firm such as PMM has responsibility for the operations or management of a company such as NSMC. An auditor must ascertain that the financial statement in question, such as the figures or the footnote, fairly presents the results of the operations and the financial position of the company. Also, as stated heretofore, in effect, an auditor must honestly believe that that financial statement or statements are neither false nor misleading in respect to material facts.

Perhaps the critical issue in this case, therefore, can be summarized as follows: Were the quoted earnings figures and footnote set forth in Count 2 fairly set out? That is to say, did they fairly present the revenue and earnings picture for NSMC for the fiscal year 1968 and the first nine months unaudited of fiscal 1969?

If you determine that there is nothing materially false or misleading about this information as alleged

in Count 2, that would end your inquiry and you would be obliged to acquit both defendants.

On the other hand, should you find that the quoted material is substantially inaccurate and misleading in whole or in part, then you would have to turn your attention to each of the defendants to consider what the evidence shows that he did or failed to do and to determine whether or not he participated in a scheme to knowingly and intentionally permit the submission of earnings figures known to be false in a material way to the SEC in the proxy statement.

End 12B

If you find that such a scheme has been proved and if you determine that there is some evidence that a given defendant participated in this you still have to ascertain, of course, that the prosecution has established beyond a reasonable doubt that the defendant under consideration knowingly and wilfully either put or caused to be put false or misleading material facts into that proxy statement or knowingly and wilfully assisted in this conduct with a realization of what was going on and a desire to participate in this scheme.

If you find that a given defendant participated simply through carelessness or negligence, with a mistaken but nevertheless honest belief that his participation was correct, truthful and sufficient, then you should acquit that defendant.

If, on the other hand, you find that the defendant in question knew that the false or misleading data of a material kind were being placed in the proxy statement and then knowingly and intentionally did something to assist in this course of action you should find that defendant guilty.

Now, you know from my recitation of the essential elements that there is no obligation on the prosecution to prove motive on the part of a given defendant

as such.

However, as a practical matter, at the very least, motive does or may come into your consideration of the cass. Even though the prosecution does not have to prove motive to establish guilt, this does not mean that you cannot consider motive or, more precisely, evidence of motive or lack of motive in determining a defendant's intentions or knowledge.

Now, normally it is said that people don't usually violate the law, in the context of this case, they don't knowingly and intentionally file false financial information with the SEC, unless they have a reason or motive to do so.

At the outset in its opening the United States Attorney conceded that the Government has no evidence that either defendant directly benefitted in the financial sense from their alleged conduct. In fact, I do not recall any evidence of direct material again either received or, indeed even contemplated for either Natelli or Scansaroli.

However, the prosecution argues that there were some substantial human motives outside of direct material gain for the conduct of both defendants. For example, as you know, the Government argues that the defendants were well aware that PMM and their own local office of

PMM had acquired what looked like a very promising retainer that of NSMC, and that this retainer looked like it would be an important and perhaps profitable one, and that the defendants were well aware that they were performing a substantial role for their own firm in servicing this retainer and that they were very anxious to assist management, even to the point of aiding and abetting management filing false earnings figures with the Securities and Exchange Commission.

Another argument the prosecution puts forward before you is that another motivation existed for both of the defendants. That argument goes something like this: The Government concedes that at the outset, in 1968, Natelli and Scansaroli didn't do anything criminally culpal On the other hand, the Government does contend that both men were guilty of a lax, negligent auditing of the 1968 figures and that as time unfolded into 1969, they well knew that their lax methods had been proved, because there they were in the midst of a writeoff of a substantial amount of the 1968 contracts which produced in the 1968 figures substantial revenues, and there came a time, according to the Government, that both men were motivated to put false and misleading statements in the proxy statement filed with the SEC so that neither the SEC nor anybody else, including

other partners in Peat, Marwick, Mitchell, would know the extent of their carelessness and laxity.

On the other side of the coin, as you well know, the defendants argue that this just isn't so, that it is absurd, and that they had no such motivation whatsoever, they were doing an honest job. They realized their problems or the problems of NSMC, but they were doing their best as professionals to work those out in an honest, good faith manner.

Well, I need not belabor the point any further. I do say to you that even though the Government does not have to prove motive as such, you may consider any evidence in the case which in your judgment shows motive or lack thereof to commit the offense here charged.

Now, I come virtually to the end of my remarks, but there are some important things still which I must take up with you. As the lawyers have fairly argued to you, you and you alone, not the lawyers, not the witnesses, not the Judge, decide the credibility of witnesses who appeared here and the weight which their evidence deserves.

In that important exclusive role of yours, you are entitled to and indeed you should consider such matters or criteria as the demeanor of that witness as he sat here on direct and cross and gave his evidence.

Second, you should consider the strength or weakness of recollection of that witness for past events. Consider any motive that that witness might have to lie or obfuscate the truth. Consider the interest which the witness has in the outcome of this case, that is to say, your verdict. Consider and compare the testimony of one witness as against other evidence in the case, documents or other witness' testimony on the same issue. These and other obvious criteria that you would use in sizing up a person with whom you were dealing in your own daily lives are the criteria to use in deciding whom to believe and whom not to believe in this case.

In summary, you are entitled under the law to accept or reject wholly or in part the testimony of any witness who appeared here during our trial.

Now, while I am on the subject I want to make another few points about witnesses. You remember that Bernard Kurek came in here and testified that he has already pleaded guilty to certain counts in this indictment. You know also that he is named in this very count in which the defendants Natelli and Scansaroli are named, Count 2.

Kurek, therefore, is what lawyers often refer to as an accomplice witness. I am not sure that the defendants contend that he is lying in all respects. As

a matter of fact, I believe, if I understood them, they would accept that in certain respects he said things which they believe are true. But in any event, I believe they contend that Kurek is lying in this case for motives or selfish reasons of his own.

Now, it is true that under Federal law, at least, a conviction can be obtained on the uncorroborated testimony of a so-called accomplice witness. The Government doesn't contend that they rely on Kurek alone. They point to documentary evidence most particularly and the testimony and other evidence which they say corroborates Kurek and stands as independent proof in any event.

However, let me point out to you, although that all my be true and that may be the law, you should scrutinize the testimony of Kurek with great care. Ask yourselves such questions as these: Would Kurek, knowing that he is awaiting sentence by this Court on his plea of guilty, come in here and think that maybe if he tailored his testimony, told a few lies in a way which might help the Government, that maybe that might make a more favorable sentence for him? I am not saying to you that he did that, but you should ask yourselves whether or not he might have done it.

He is a witness who, of course, was a management figure in NSMC, and just because he is an accomplice

doesn't mean, on the other side of the coin, that he is incapable of telling the truth.

However, I think it is only fair that you should consider the point I just made and more generally scrutinize his evidence with particular care.

Now, there was another kind of witness, in fact, there were a number of them who appeared here, and they are what the law calls character witnesses. As you know, both defendants produced a number of witnesses who testified about their knowledge of the reputation of the defendants and told us what that reputation was.

That type of evidence is perfectly proper in cases of this kind. Indeed, evidence of good character in itself might create reasonable doubt in your minds if you were so inclined to accept it and credit it. Even though that is true and that is the law, I point out to you on the other side of the coin that in life we know that persons of previously impeccable reputations sometimes do fall and get convicted of crime. But in weighing those considerations I point out to you that you certainly are entitled to consider that character evidence, and if you choose to, weigh it in the balance sufficient to create a reasonable doubt in your minds on the guilt of one or the other of the defendants.

Now, I believe, before I pass witnesses, that there was an argument or there may have been an argument that the Government didn't produce certain witnesses that they could have produced and should have produced. If you recall that such an argument was made, I point out to you this proposition of law:

If it is particularly within the power of either the prosecution or the defense to produce a witness who would give relevant testimony on an issue in the case, failure to call that witness might create the presumption that his testimony would be unfavorable to such a party. However, no such presumption should be drawn by the jury where the witness is equally available to all parties or where the witness' testimony would be merely cumulative.

Now, the Government would argue in this context that if it is contended that they didn't produce some of the other defendants who you know have pleaded guilty in this case or perhaps other people representing some of these oral contract clients, Eastern Airlines, Pontiac, or whatever, the Government would argue to you that those people are just as available to the defendants as they are to the Government and therefore you should bring no such inference to bear against the Government at all.

I point out to you that it is up to you. You can

either draw such inference or not, as you see fit under the circumstances.

Now, one of the forms of evidence in this case is what were called charts. As you know, the Government put in a number of charts. I believe the defendant Natelli put in at least one chart. Chart evidence is not unknown in cases of this kind. In fact, it is quite usual in cases of this kind that chart evidence comes in.

I point out to you -- and I said this to you before you will remember -- that charts, however, are to be regarded as aides memoire, and by that I mean very simply that charts are only intended by the party offering them to be summations of just certain evidence, not all of the evidence. Therefore, if you view a chart as not supported by direct evidence in the case, either documentary or testimonial evidence, then you should pay no attention to that chart at all.

If, on the other hand, you find that a chart is based solidly on direct evidence in the case, and you consider the chart to be helpful and relevant, you can consider it as an aide memoire in your deliberations.

As you I think have been told, you should not even consider the possible question of punishment, that is to say, the question of punishment in the event you were to

determine one or both of the defendants guilty. Under our system it is true that sentencing or punishment is exclusively the function of the Court.

Therefore, I ask you not to consider punishment or possible punishment at all in your deliberations in this case.

Now, finally, I will say to you that we will ask you to return a general verdict in respect to each defendant under count 2. Your verdict must be unanimous, that is to say, you are to tell us when you complete your deliberations whether you find the defendant Natelli guilty or not guilty of this charge. Similarly you report through your foreman, Mr. Lights, whether you find the defendant Scansaroli guilty or notguilty of this charge. Your verdict either way with respect to the defendants must be unanimous under our system.

Now, I unfortunately have had to cover a lot of ground and I have gone beyond the time I estimated. You have been most patient. I am going to ask you to take a recess, however. I want to give the lawyers a chance to comment upon my instructions. Perhaps I said something unwittingly that was incorrect or I left out something. In a few minutes we will have you back and commit the case to you. We will ask you now to take a brief recess.

(Jury left the courtroom.)

THE COURT: Mr. Velie, any exceptions or supplementals?

MR. VELIE: No, your Honor. The Government feels that the charge was right down the middle and fair.

THE COURT: Mr. Martin?

MR. MARTIN: Yes, your Honor. First, on the summary of contentions, I think inadvertently your Honor left out our summary in toto with regard to the booking of the Eastern commitment. You did give the Government's contention as to that, that this all occurred at 3 o'clock in the morning. Our contention had pointed to the fact that the testimony was that decision wasn't made until the following week.

THE COURT: You pointed to one strand, but I point out to you two things. I told this jury I wasn't covering every contention. I left out a great many of the Government's too.

MR. MARTIN: I realize that, your Honor. It was only the fact that you did go into the Government's contention on this point and not to ours that caused me to raise that issue.

THE COURT: All right. I will consider that. You are right, I know. My eyes went over it.

MR. MARTIN: I understand that, your Honor. It

the fact that the Government's came out that way.

THE COURT: All right.

MR. MARTIN: Two, simply to preserve my record, your Honor, I want to object to the Court's charge on the issue of whether or not a proxy was a document required to be filed.

THE COURT: I don't understand that issue. But you are right, you have raised it. I never understood you and I still don't understand you.

Is there any doubt in your mind that either of these defendants had any doubt at all as to what they were working on? I don't understand you.

MR. MARTIN: Oh, no, not at all, your Honor. They knew they were working on a proxy. I am simply making an argument that in construing a criminal statute it must be strictly construed and there is no statute that says you must file a proxy. You only have to file a proxy -- the only crime set forth is soliciting when a proxy is not on file. It is a technical argument, your Honor.

THE COURT: I don't mind technical arguments, Mr. Martin, but this strikes me -- and I don't meant to accuse you accordingly -- it sounds to me like a shell game. I look for the peanut and thenwhen I find it you say it is not there.

I don't understand you. They filed this. There is not a scintilla of doubt about it. If any certified public accountant is coming into court to tell a jury or a judge that he didn't know he was working on this or that somehow, though it wasn't required to be filed, it was filed, and therefore this is an exhoneration, I don't understand you. But exception to you.

MR. MARTIN: Thank you. Your Honor, again, just to preserve my record, I would like to except to the charge on reckless disregard.

THE COURT: Yes. Exception to you.

MR. MARTIN: Your Honor, I think there was a statement in your charge when you tried to say "I think we are getting down to the important issue, whether this footnote fairly stated the financial condition of National Student Marketing."

My problem with that is that the charge is really this was a footnote to a statement of earnings and the issue is whether the financial statements fairly reflect the fact.

THE COURT: I would accept, if I understand you, that I telescoped some of this, not only once, but several times. But I am sure the jury would understand that, particularly since the indictment is so specific. There are two respects in which the Government contends that there were

material misstatements of fact. I made that point and I don't think I will say it again. Exception to your client.

MR. MARTIN: Your Honor, the next point I have is that you talked a good deal about an auditor's responsibility in doing an audit, but the May 31, 1969 proxy figures were unaudited and there was no --

THE COURT: I stated that about 16 times. The significance of that is not lost on me, and I hope by this time is not lost on the jury. That is also why I kept saying unaudited first nine months figures of 1969. I insist I repeated that ad nauseam. It is because of little details like this that the charge lasted so long in fact.

Exception to you.

MR. MARTIN: The other, I would ask your Honor to charge the jury -- you did mention that they could find either statement to be false -- I would ask your Honor to charge the jury that though that is true, they must be unanimous as to which statement is false.

THE COURT: I think that's clear from what I have already said and I won't say anymore about that. Exception to Mr. Natelli.

MR. MARTIN: The final thing, your Honor, your Honor in summarizing really a Government argument said that there was an argument that Peat, Marwick had received a

retainer here, that was important to these defendants. There has never been such an argument, there has never been any record as to fees on this engagement.

THE COURT: Perhaps I didn't put it as well as I could in hindsight, but that is not the real thrust of what I was saying.

I think at the very least it is implicit in the Government's submission that these men were aware this was an important account. Why not? They were entitled to be aware of it. Nothing wrong with that. It is just another way of stating the way Mr. Velie puts it, that there came a point where they were trying to cover up. I just put it in a different way.

I am sorry. I speak differently than you and Mr. Velie and Mr. Stillman. I don't think it was an unfair statement, however, and I refuse to charge further on that.

MR. MARTIN: Thank you, your Honor.

retainer here, that was important to these defendants. There has never been such an argument, there has never been any record as to fees on this engagement.

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MR. MARTIN: Thank you, your Honor.

than that. No one can prove motive directly.

MR. STILLMAN: But the point is, Judge Tyler --

THE COURT: They are bare bones facts. I don't want to discuss it. Exception to you.

MR. STILLMAN: All right, sir.

Your Honor, I don't believe that at any point in the charge you advised the jury with respect to the aiding and abetting statute --

THE COURT: I didn't. I purposefully left it out. The more I thought of it, the worse it sounded. I really think it is a disadvantage, perhaps from the Government's point of view, more serious for them than it is for the defendants. What I did do, however, and I did it having in mind one of your requests, I gave them in substance, although I would be the first to say not as eloquently as the Court did it in such a celebrated case as U. S. vs. Peoni, a case known by heart to all former assistant United States attorneys, like you and me -- I didn't go into the clankety clankety, clankety which is customarily done here with the iron-fisted discussion of the statute. That's true, I didn't. I refuse to go any further. I'm frank to say that I'm surprised you would raise it. I rather thought Mr. Velie would.

MR. STILLMAN: All right, sir.

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The other point I wanted to make, your Honor, our request number 3, which is the one that advises the jury that they should accord the Government no greater weight merely because it is a party to this lawsuit --

THE COURT: You are right. I didn't put that in. Exception to you.

MR. STILLMAN: I came in second on that one again, your Honor.

THE COURT: That's just language, in my opinion. It really goes to the burden of proof. I know that judges give that charge. It is not my style and, therefore, I will give you an exception.

MR. STILLMAN: I have nothing further, your Honor.

THE COURT: Now, Mr. Martin, I need your help. I have never quite understood. Maybe that's one reason why I didn't hit Natelli's argument. I'm frank to say I don't understand it.

MR. MARTIN: On the Eastern --

THE COURT: I'll give anything within reason, yes.

MR. MARTIN: Simply that Mr. Natelli did not simply accept theletter and agree to the booking of the Eastern commitment at the printer. He obtained the presentation from Mr. Kelly, reviewed that, went back to Washington.

got the time sheets of Mr. Bushnell, reviewed that.

THE COURT: Yes. I'll tell you what's always bothered me about that, the figures were the figures.

MR. MARTIN: Your Honor, I think it goes to the question of whether or not he made an investigation to determine whether thiswas a real contract.

THE COURT: After the fact.

MR. MARTIN: No, the figures were then reprinted the following week.

THE COURT: No, I'm sorry, you are right. Okay, I get you.

MR. STILLMAN: Also, your Honor, it is supported by the testimony of Mr. Buck to the effect --

THE COURT: I read Mr. Buck last night. I don't want to get in an argument with that. I don't think that necessarily is true. I don't want to argue with a nice fellow like you about that one.

MR. VELIE: Your Honor, if you are going to give a further contention of the defendant at this late hour right before the jury goes to work, I believe it would only be fair to put it in context by giving back a piece of the Government's contention which goes on this item of proof.

THE COURT: Mr. Velie, you sit down and listen and you may be agreeably surprised.

MR. VELIE: Thank you, your Honor.

THE COURT: All right. Bring in the jury.

MR. STILLMAN: Is the program to send them to lunch now --

THE COURT: They have been a patient group. I'm going to send them to lunch.

MR.STILLMAN: Over the luncheon we can pull together the exhibits as you had requested and they should be there waiting for them when they come back from lunch.

THE COURT: That's what I would like. That's what I meant, exactly.

(Jury present.)

THE COURT: Mr. Light, and ladies and gentlemen, before we commit this case to you, there is just one thing.

Counsel has brought to my attention, and I think correctly as I recall it, that when I was summarizing the contentions having to do with the Pontiac commitment being removed from the books and the Eastern commitment being substituted up here at Pandick Press, that I only summarized the Government's contentions and not those of Natelli and Scansaroli.

I think that is right.

As you know, Scansaroli has testified that he was not a participant in that discussion and I don't recall that any witness said to the contrary. So, therefore, he says he was not directly involved.

Natelli points to his testimony to the effect that though he agrees that he first heard about Eastern in mid-August, and most significantly really in the early morning hours at Pandick Press, he didn't just lightly accept this account, and he testified that he went back to Washington from the Pandick Press business, that he asked for time sheets from Mr. Bushnell, who was an officer and account executive at NSMC, who apparently purported to be the NSMC account executive who obtained this commitment,

and that he looked into it very carefully before he approved the inclusion of the gross revenues from the Eastern contract in the figures for the proxy statement.

As you know, the Government says that that evidence isn't persuasive at all. The Government argues that Buck's testimony was that this was really decided at Pandick Press and that Natelli's testimony of his checking into this carefully is not to be believed and was not sufficient to carry the day on this issue.

I need say no more. I think you understand both both of those arguments essentially.

I am going to have the marshals sworn and then we are going to have you go out to lunch at the expense of the United States. Then you will return and take up your deliberations.

While you are gone we are going to arrange to have all the exhibits put in your jury room so that you can refer to them as, and to the extent you wish, that is the Government exhibits and the defense exhibits.

While you are at lunch I don't want you to deliberate at all. I want you to relax and enjoy your lunch. Then you come back. Only commence deliberations when you get into your jury room.

MR. MARTIN: Could I see your Honor at the side

bar?

THE COURT: I would rather not. I don't know any reason why.

MR. MARTIN: I would like to point out a matter in the transcript that relates to what your Honor just advised the jury.

THE COURT: Come up.

(At the side bar.)

THE COURT: What is this weighty issue?

MR. MARTIN: I believe your Honor advised the jury that Mr. Buck testified that the decision on Eastern was made at Pandick. I would like to refer your Honor to --

THE COURT: I didn't say that at all, Mr. Martin. I said that the Government argues. Now, it is not my job to decide this case, and I believe I have been scrupulously fair. I said no such thing. If we are going to pick every detail apart in this case, we are never going to get anywhere.

MR.MARTIN: I am sorry, your Honor. I thought you said --

THE COURT: I said the Government relies on the Buck testimony to argue that. I think that is a fair statement. I am only making contentions. I am not

jamming the evidence now in particulars like this. I take it a little bit unkindly that you have to do this to me at this hour. I don't really think that is called for. If I thought I wilfully or even innocently misstated something, I would be the first to agree.

I don't believe it.

(In open court.)

THE COURT: Before we go any further, ladies and gentlemen, it is my duty to excuse and say goodbye to Mrs. Immendorfer, Mrs. Spiro and Mrs. Aronson. Under our system it is required that you be excused at this point. I am sorry that you cannot remain through to the end, but I want to salute and thank each one of you. I think all the parties and counsel would agree that you have been valued participants who have listened carefully and have been here punctually, for which we collectively thank you and wish you God speed. You are now excused.

(Alternate jurors excused.)

(Two marshals sworn.)

THE COURT: Now, ladies and gentlemen, you may retire in the custody of the marshals. As I say, you will first be taken to lunch. Do not begin to deliberate until you return from lunch.

(Luncheon recess.)

AFTERNOON SESSION

(At 3:50 p.m. a note was received from the jury:)

"Your Honor: Could we possibly have in writing the portion of your charge that pertains to material and false statements and knowingly and willingly."

(In open court.)

THE COURT: Gentlemen, have you seen this note?

MR. MARTIN: Yes, your Honor.

MR. STILLMAN: We have, your Honor.

THE COURT: That note will be marked for identification as Court's Exhibit 5 and included in the record as such.

xx (Court's Exhibit 5 marked for identification.)

(Jury present.)

THE COURT: Mr. Lights and ladies and gentlemen, we have your note. I am not entirely sure that I understand you, so perhaps I better ask.

There was a point where I talked to you about what you do when you come to decide whether or not a fact is material or what is a material fact within the meaning of the law and I assume that that's the last part of what you

want, is that correct?

You also asked me to talk again about knowingly and wilfully, what the law means by those words or that phrase.

Of course, I talked a great deal about that in various portions of my charge or instructions. What I intend to do is read what I think you have in mind and then I will ask you again to make sure I have covered what it is that you wanted.

I am embarrassed to say that I rushed down without my glasses. If you will just be patient a minute, I will read I think a little bit better than I would without.

I think, however, I can begin, even though my law clerk is coming, I am sure. Let me repeat something. I will instruct you once again, as I did this morning, on what a material fact is conceived to be by the law.

Incidentally, you asked if it was possible that you get this in writing. Under our system that's not possible. I will be obliged to orally do it again.

Let me repeat what I said this morning. I said that in deciding whether a fact is material you are entitled to consider whether it is the kind of information that a financial statement ordinarily contains in order to fulfill

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its function of fairly presenting the financial information or data in regard to the company or corporation in question, in our case, of course, NSMC.

I also defined a material fact as follows:

A material fact can be simply defined as one that would matter to a reasonable person in deciding whether or not to purchase stock, such as shares of stock in NSMC, that is to say, a fact the validity of which would concern a reasonable person in making his purchase or investment decision about the company in question.

I went on to say that obviously a balance sheet or income statement or data is not supposed to contain all of the information a creditor or a potential investor or stockholder might want to know or see in order to make an informed judgment. The function of the financial statement or an income statement is simply to present a basic summary of the company's essential financial position and its operations and earnings for the time or period stated or in question.

In this regard I went on to say parenthetically that outside auditors such as Peat, Marwick, Mitchell of course have no responsibility for the operations of management of a company such as NSMC.

On the other hand, an auditor must ascertain when

he is working on materials such as a proxy statement for a company that the financial statement in question, including such figures which are relevant or a footnote or footnotes that might be relevant contained therein, fairly present the results of the operations and the financial position of that accounting firm's client. Also an auditor must honestly believe that the financial statement is neither false nor misleading in respect to material fact as I have defined material fact.

Now, am I correct in understanding that this is part of what you want in your note?

JUROR NO. 1: I think I am at fault for having been ambiguous.

THE COURT: No, no. That's all right.

JUROR NO. 1: The area in question had to do with the four points you outlined at the very end of your charge.

THE COURT: The essential elements?

JUROR NO. 1: Yes.

THE COURT: That is what you would like?

JUROR NO. 1: Yes.

THE COURT: All right, sir. I will turn to the essential elements.

As You stated, there are four essential elements which the Government, as it well knows, must establish

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beyond a reasonable doubt.

The first essential element is this, that NSMC filed a proxy statement with the SEC which was required by law so to be filed, and as I pointed out this morning, I do not believe there is any substantial issue about that, and indeed I will instruct you that since NSMC was a registered company, as the law defines that term, they would be obliged to file a proxy statement, as they in fact did under the circumstances pertaining in September 1969.

The second essential element is that some statement made in the proxy statement was false or misleading as to a material fact. Specifically, as you know from the allegations of count 2, the Government contends that there are two portions or two statements in the proxy statement, Government's Exhibit 25, which are set forth verbatim in count 2, are false and misleading as to material facts.

The third essential element is that the defendant made or caused to be made the false or misleading statement or statements.

The fourth essential element is that the defendant in question in so doing acted wilfully and knowingly.

Those are the four essential elements which the Government must prove beyond a reasonable doubt in order to support a conviction.

Now, is there anything further that you would like repeated for you?

JUROR NO. 1: Wilful and knowingly.

THE COURT: All right. Very good.

I repeat what I said in substance this morning. In the context of this case, ladies and gentlemen, a defendant may be found to have acted wilfully and knowingly only if he knew that a portion of the financial statement, such as the footnote or the financial data entries there that are alleged in count 2, was false and misleading.

It is not enough to prove, in other words, that he was acting knowingly and wilfully if all the evidence establishes is that a defendant under question acted negligently or carelessly. I pointed out that although mistakes or negligence might give rise to a civil lawsuit, they do not constitute a sufficient basis for finding criminal or culpable conduct.

A finding of an intention to include false or misleading information of material nature is required here in order to find that a defendant acted wilfully and knowingly.

Good faith, that is to say, an honest belief in the truth of the data set forth in the footnote or the other entries which are alleged in count 2, would not be

proof of any knowing and wilful intention to do something misleading in the way of setting up entries or footnotes in these financial statements and thus support a criminal conviction.

Now, it is true, ladies and gentlemen, that in a great many other portions of my charge I was in part talking about knowing and wilfully. But that is the sum and substance of it as I stated this morning. But again, I ask you, is there anyone or more of you who would like anything more either on this subject or on some other subject in this area, generally speaking?

Does that seem to be about it?

All right. Very good. You may retire once again and take up your deliberations.

(At 4:12 p.m. the jury left the courtroom.)

MR. VELIE: Your Honor, I omitted to request it while you gave your portion of the charge, but it occurs to me now that a portion of your charge about reckless indifference is a portion of your charge having to do with what they asked about.

THE COURT: Mr. Velie, that was in a sense what I was trying to ascertain. There were a lot of things that bear on this peculiarly worded note. This is a typical problem, and I don't mean this in criticism of Mr. Lights

or a. other juror. But my view of the matter is that what should be done is that the Judge should ask them what they want and as best as he can respond to what they say. They indicated at the end that they had nothing else they wanted. Hence I stopped. There was a lot of material that I could have gone back and repeated. Who knows, maybe down deep in somebody's mind you are right. But it didn't come out that way and there the matter must rest.

MR. VELIE: Thank you. I just wanted to give us the opportunity to do it.

THE COURT: I understand.

(At 5:20 p.m. a note was received from the jury.

(In open court; jury absent.)

THE COURT: Gentlemen, we have a note, which will be marked Court's Exhibit 6. The jury is on the way in.

Let me briefly say that they want some testimony apparently about the Pontiac commitment and the substitution, so-called, of the Eastern commitment therefor.

I propose that we do this tomorrow. It will probably constitute the need for digging out exactly what they want. The note is somewhat difficult for me at least to determine with any certainty exactly what they want. Rest assured you will have a chance to see it before anything of significance is done.

(Jury present.)

THE COURT: Mr. Lights and ladies and gentlemen:

We have your last note, of course.

From what I understand, you are not about to reach a verdict very shortly this evening. If I'm correct in that assumption, I propose to send you home with instructions and have you come back in the morning, at which point we will endeavor to have read to you the testimony about what you seek.

Now, taking up the latter first, I gather that

what you would like is to hear and have reread to you the testimony of those witnesses who talked about the Pontiac and the Eastern commitments down here at Pandick Press in August of '69.

My memory, for example, is that Mr. Buck talked about this, Mr. Natelli, of course, Mr. Kurek, I believe, perhaps others.

Would you like to hear their testimony on those subjects? Is that what you are really seeking?

THE FOREMAN: Yes.

THE COURT: All right.

Then here is what we will do. This will take some digging out, even though we are fortunate to have the transcripts here. It still will take some time.

What we will do is suspend now until tomorrow morning and we will start the morning with that.

I'm going to ask you to go home, and I want you to keep, however, a couple of important points in mind. I'm sure they will be obvious to you and the importance thereof will be obvious to you. Nevertheless, they are worth stressing briefly.

First of all, when you go home now don't talk about this case or particularly about your deliberations or any part of them with anybody. That means family, friends,

whatever. Your deliberations are your business and your business alone. Nobody else should know about them.

And then tomorrow when we complete this reading of the testimony which you seek, you should go back, take up your deliberations of course exactly where you left off. In short, put the case entirely out of your minds, out of your thoughts, out of your words when you go home until you return tomorrow morning.

Second of all, and I stress I have absolutely no reason whatsoever to think that this will happen, but a word of caution, nevertheless, maybe in order.

If somebody approaches you and asks you anything about this case, you put them off and refuse to say anything. Now, I mean that. I don't think anybody is going to do this, but I just want to be excessively cautious and tell you that that's the way to handle that if it should occur. More than that, if anybody should try to approach you over the evening recess, I would like you to tell me about it privately tomorrow. Again, however, I don't think anybody is about to approach you as you go to and from your homes between tonight and tomorrow morning.

All right. I'm going to ask, if you will, to come back to your jury room tomorrow morning at 9:30. I'm hopeful that the lawyers will be able to assist the

reporter in digging out the portions so we can read it to you without any delay.

Have a very good evening. See you tomorrow at 9:30. Incidentally, when you come in at 9:30, go first to your jury room. I will be here. We will get you in a few minutes thereafter when we are ready to read the testimony.

All right, have a good evening.

(Jury excused until November 14, 1974 at 9:30 a.m.)

THE COURT: Gentlemen, obviously this note, in substance, you know what they mean by it apparently. However, it is a two-page note and it is certainly to be read by you now. I wish you would do that.

Second of all, I'm going to mark as a Court's Exhibit a letter which I wrote at the request of Juror No. 4, Mr. Charles Hajek. You remember he's an employee of Con Ed. He was concerned that his supervisor thought that he might be on a frolic rather than sitting in our jury, and I have written the great man a letter to assure him that Mr. Hajek has been very busy and still is. That will be marked as a Court's Exhibit, and of course, is available for your scrutiny if you care to read it.

Now, I would suggest that perhaps now you could spend a little time. I think I was accurate as far as I

went, but it may have been some other witness testified about Pontiac and Eastern, but I believe it was Kurek, Buck and Mr. Natelli essentially.

Am I wrong?

MR. VELIE: Your Honor, Mr. Scansaroli was asked about the subject and my recollection, of course, is that he denied any knowledge that it happened.

THE COURT: That's right.

MR. VELIE: I believe that that is relevant material in this area as well.

THE COURT: That may well be.

I would suggest that the three witnesses they really want to hear from what they said when they were just here were the three named. If there's anybody else, of course.

Now, I have a full set of transcript here. You all have a set. I would suggest that it might be a good idea if you came in about 9 o'clock tomorrow morning, or would you prefer to do it now?

I don't care.

MR. MARTIN: Your Honor, why don't we dig it out tonight and meet with you at 9:15 and we will have it.

THE COURT: I'll be here. Fine. Very good.

(Court's Exhibits 5 and 6 marked.)

(Adjorunment was taken to November 14, 1974 at 9:15 a

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UNITED STATES OF AMERICA

vs.

ANTHONY NATELLI
JOHN SCANSAROLI

November 14, 1974
9:15 a.m.

(In the robing room.)

MR. VELIE: Your Honor, the Government proposes a little bit more reading than Mr. Martin wanted to have read. I think probably the simplest way to do this is I'll say what it was that I had in mind by witness and Mr. Martin can say what it was he had. We have a transcript here. I think it would be a good thing if you took a look at it.

Kurek's direct, I propose reading from 255 to 26[illegible], which covers the Pandick Press incident, and his cross examination at pages 539 to 545, 547 and 548 and one little piece of his redirect, page 572.

Mr. Martin has some different ideas about Mr. Kurek.

THE COURT: This would be what day?

MR. VELIE: I have it right here, your Honor.

MR. MARTIN: Judge, it might help the discussion if I simply stated my basic position.

It seems to me that the jury has sent in a note indicating a confusion as to a particular issue in which they said, could we hear just enough pertinent testimony to clear this up.

THE COURT: In thrust I agree with you.

MR. MARTIN: It seems to me that the question they ask, the pertinent testimony, there are two ways of doing this.

THE COURT: First of all, my recollection is that Kurek went into this and really can't be ignored. I assume you agree.

MR. MARTIN: Yes.

THE COURT: What is it that there is the difference about?

MR. MARTIN: Your Honor, I think the transcript relating to the question that they asked, which is, was the decision made at Pandick Press or was it made the following week, is found solely in Kurek's cross from 539, line 22, to 541, line 23.

THE COURT: In other words, you would like to limit Kurek to cross only?

MR. MARTIN: That's right, your Honor.

THE COURT: You would start at the bottom. You don't want to go into this thing about diversified data?

MR. MARTIN: Line 22, your Honor.

THE COURT: Right.

(Pause.)

MR. MARTIN: I was ending at 541, line 23.

THE COURT: There's no doubt about that?

MR. MARTIN: There are two possible ways of doing it. We can try to go into everything said about Eastern and Pandick. Mr. Velie will only want all direct and I'll want all kinds of cross. What I'm proposing, your Honor, I think the portions that deal directly with the questions asked by the jury. I have calculated it out. Doing it one way you come up with 59 pages of testimony, doing it the way I suggest you come up with 12 pages of testimony.

MR. VELIE: I would like to respond to that.

THE COURT: Wait a minute. Before you do let me have back the part that you --

MR. VELIE: 255, your Honor.

THE COURT: Continuing over to what page?

MR. VELIE: It goes to 263, eight pages.

(Pause.)

THE COURT: 255 to what?

MR. MARTIN: 263.

MR. VELIE: 263, your Honor.

THE COURT: If this is the dispute, I think that

would like to look one more time at the note.

MR. MARTIN: That's our copy of it, Judge. We wrote it out. I think it is important to consider what the jury asked.

THE COURT: Thank you very much.

Well, I can see your interpretation of the note Mr. Martin, and I can see a number of other possible interpretations, but I believe the Government is entitled to have this read.

First of all, I'm not entirely sure that the jury wants to exclude what Kurek said on direct at all.

Second of all, I feel that there's a real ambiguity in the record as to just what happened on this. I'm not accusing anybody of misstating or being a liar or anything like that. That's not my function.

It is just that the way it came out, it is very hard to tell when you think about all of this just when the agreements were made and what happened later in Washington when the accountants went back and the management people went back. I don't think that it is at all unfair or prejudicial to anyone to try and answer that.

As a matter of fact, when we get through I am going to follow my usual practice and flatly ask the jury, does that cover it? Is there anything else that we may ha

overlooked that you can think of? If so, please say so.

So I will rule in favor of Mr. Velie on this one.

MR. MARTIN: Your Honor, if that is the ruling, that we are going into a broader matter than I had proposed then there are obviously additional lines of cross examination that I would want covered in that.

THE COURT: I'll tell you what we will do. Here it is 9:30 already. You are talking about Mr. Kurek?

MR. MARTIN: That's right.

MR. VELIE: I think we may actually be very close to agreement on this. 539 to 548?

MR. MARTIN: 515, line 21 to 519, line 16.

(Pause.)

MR. MARTIN: Velie has no objection to that. Then 534, line 1 to 535, line 5.

THE COURT: Wait a minute. Line 1 on 534, the question was objected to and sustained.

MR. MARTIN: Starting under that, your Honor.

THE COURT: I don't see any point in that. What else is there?

MR. MARTIN: 534, starting under that, to 535, line 5.

THE COURT. I don't see any objection to that.

MR. MARTIN: Then 539, line 22 to 541, line 23.

MR. VELIE: I thought you should go from 539 essentially to 548. There's a break for colloquy.

That's giving you more of your cross examination than you wanted.

MR. MARTIN: It could go further. I'm happy to stop at 541, line 23.

THE COURT: I don't see any objection to that. I think that's very pertinent.

MR. MARTIN: 624, line 6 to 12.

MR. VELIE: Before we go to 624, I'd propose that we go to 548,

(Pause.)

THE COURT: Excluding all the colloquy and rulings, I would agree you could go to 548, although actually most of it is colloquy.

MR. MARTIN: Most of it is him saying he doesn't know about things. Particularly in light of what the jury asked, I would not like to confuse them by going further.

THE COURT: I don't think that's the point. We can't restructure witness' remarks. The jury has picked to filter just this kind of thing out in my judgment. Therefore, I would say let's go to 548.

What else, Mr. Velie? Is that it?

MR. VELIE: I think that's it except for Mr. Buck.

THE COURT: I thought you agreed on Mr. Buck.

MR. MARTIN: Your Honor, I had the same thrust before. In view of your Honor's ruling as to Kurek, then I think we go back, 651, line 10 to 655, line 7. The cross would be 672, line 13 to 683, line 4. There's agreement on that, your Honor.

THE COURT: Is there anyone else beside Mr. Buck.

MR. VELIE: Mr. Natelli.

MR. MARTIN: And Mr. Oberlander.

THE COURT: I assumed you agred on those.

(Pause.)

MR. VELIE: Your Honor, there's a slight disagreement between Mr. Martin and myself respecting three pages in which Mr. Natelli says that he heard of Eastern before he went to Pandick Press. It is 1913 through 1916.

THE COURT: Yes, I remember that.

You think that should be excluded?

MR. VELIE: Yes, your Honor.

THE COURT: No, I disagree.

MR. MARTIN: 1913, line 23 through 1931, line 10.

THE COURT: Is the jury here?

THE CLERK: Yes, your Honor.

MR. VELIE: I end at 1930, Mr. Martin ends at 1931. Your Honor will recall that speaks only to a question and answer about whether he intended to defraud anybody about Eastern.

THE COURT: I don't think we need that. We all know what his testimony is on that.

MR. VELIE: I think the actual testimony on the subject --

MR. MARTIN: The only question I would add your Honor, "at the time the conclusion was reached, did you believe it was appropriate for the company to record the commitment."

"Answer. Yes, sir."

THE COURT: Did you believe it was what?

MR. MARTIN: Appropriate for the company to record it.

THE COURT: That is permissible.

I thought thiswas all agreed. You told me the only conflict was Mr. Kurek.

What was all this time invested last evening?

MR. STILLMAN: We were working independently. That's what happened.

THE COURT: I see.

MR. MARTIN: Your Honor, I think there is some question as to whether or not all this cross from 2047 to

2055 should be concluded.

MR. VELIE: 2059. All it really excludes is a few pieces of colloquy. I have it available for the Court. It amounts to about ten or 12 pages, I believe.

THE COURT: What's the dispute here?

MR. MARTIN: The dispute is, your Honor, whether or not it is appropriate to include, given this request, all of these questions, while Scansaroli was in the room, Scansaroli was this, Scansaroli was that. This is a question directed to Mr. Natelli's decision.

MR. VELIE: I'm not so sure of that.

MR. STILLMAN: The language is so completely clear on that.

THE COURT: Gentlemen, that's not the point of this exercise. We are not here to make the decision in this case. The defendants have a jury here for that purpose, so does the Government.

MR. STILLMAN: I appreciate that, your Honor.

THE COURT: I'm going to allow this.

MR. STILLMAN: May I just note most respectfully, Judge Tyler, my objection to that on the ground I don't think that in any way sheds any light on the specific request that the jury has asked for.

THE COURT: Mr. Stillman, I will say to you what

I said earlier, I do not regard jurors notes, which are to me succeptible of several constructions, to be read narrowly. I do not think anybody is prejudiced by this. I do not think that this is a fruitful exercise. Exception to your client. Bring the jury in.

MR. MARTIN: We just have to get agreement on the last matter which is Oberlander.

THE COURT: Let me suggest to you, when we come to Oberlander, if there is still a disagreement, we will come to the side bar. I want to get the jury going.

(In open court, jury present.)

THE COURT: Good morning, Mr. Lights and ladies and gentlemen.

The process of marking the pages and helping the reporter for the starting and ending points still goes on, but they will be finished in a second.

(Pause.)

THE COURT: Mr. Lights and ladies and gentlemen, Mr. Hillman will start with the reading of the excerpts which we believe applies to your request. He will read first from the portions of the testimony of Mr. Bernard Kurek, then I believe from the testimony of Mr. Buck, then from the testimony of Mr. Oberlander and I think last from the testimony of Mr. Natelli.

(Record read.)

MR. VELIE: Your Honor, the defense and the Government both agree that Mr. Natelli referred to in the last two questions must be a typographical error. It is Mr. Kelly who was being asked about it, did Mr. Kelly bring that down and so on. Why don't we reread it with Mr. Kelly's name.

(Record read.)

MR. MARTIN: Your Honor, there is something which I think should be added on that page.

THE COURT: Again, I can't respond because I don't have the transcript.

MR. MARTIN: Line 17, same page, through line 20

THE COURT: In other words, you want to add lines 13 through 21?

MR. MARTIN: That's right, your Honor.

THE COURT: All right.

MR. VELIE: As long as you have the transcript, would you please take a look at page 572 between lines 3 and 14.

THE COURT: Gentlemen, we spent a great deal of time on this. I thought we had come finally to an agreement. Looking back at this point I don't think is very helpful. Let's complete what we are doing at 624. Then if you feel

something has been omitted, at the end of the reading of Kurek we will discuss it.

(Record read.)

THE COURT: You want to consider something back?

MR. VELIE: Yes, your Honor, page 572.

THE COURT: Did you hear that, gentlemen?

MR. VELIE: 572.

THE COURT: Line 4 through 15, I think.

MR. VELIE: Yes, your Honor.

MR. VELIE: Mr. Martin says he has no objection

THE COURT: Yes, I see the point.

MR. VELIE: Thank you.

(Record read.)

MR. MARTIN: Your Honor, I think we should go to Mr. Oberlander before we begin Mr. Natelli. That was the order at the trial. There are one or two pages to be worked out on that at the side bar, which should take us on a minute.

THE COURT: All right.

(Pause.)

THE COURT: All right, gentlemen. Are you ready now?

MR. VELIE: We have all agreed, your Honor.

THE COURT: I thought you disagreed, I'm sorry.

MR. VELIE: Not at all.

THE COURT: Very good.

(Record read.)

THE COURT: Are you satisfied now, gentlemen?

MR. MARTIN: Yes, your Honor.

MR. VELIE: Yes, your Honor.

THE COURT: Mr. Lights and ladies and gentlemen are you satisfied that we have covered everything that you wanted covered?

All right. I see you all nodding.

Therefore, I will ask you if you retire once ag and take up your deliberations.

(At 11:05 a.m., the jury left the courtroom.)

(At 12:05 p.m. a note was received from the jury:)

"Your Honor: We cannot agree."

(In open court.)

THE COURT: Gentlemen, before we call the jury in, are there any views that you want to express in respect to the last note received from the jury?

MR. MARTIN: If I may, your Honor, I would renew the suggestion that I made. If your Honor is going t tell the jury to go back and deliberate, perhaps it would be appropriate before they do that to send them out for lunch, so that the jury does not get the impression that any pressure is being placed on them at this time.

THE COURT: All right. I will be glad to consid

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that.

MR. MARTIN: Also, your Honor, I would like you to consider another matter that relates to the testimony read this morning and one of the Government's charts, which does have a label on it that is misleading on that specific issue, that is, the last chart which summarizes all of the contracts on the books, and then it says Easter and the notation on that is "booked 8-15." That notation, to be more accurate, would say "information taken from a schedule of Mr. Oberlander which bears the date 8-15.:

THE COURT: I think this point was made clear to the jury. Second of all, I point out to you it is a little late to be concerned about that. Third of all, I have carefully and not idly instructed the jury that if they didn't feel that any entry or any portion of one of these charts was based squarely on direct evidence in the case they would be free to disregard it.

So I am not about to reargue and remodify past events of that kind. Exception to your client.

Now, let's turn to the matter at hand. That is what concerns me. Mr. Velie.

MR. VELIE: Yes, your Honor. The jury hasn't been working very long.

THE COURT. I agree with that. No argument there.

What is it you --

MR. VELIE: It seems to me that an Allen charge may be a help to them in understanding what their role might be in coming to an agreement, how to go about discussing things with each other in the jury room.

THE COURT: All right.

MR. VELIE: I would also ask the Court to consider either now or later, if the jury finds that they are having difficulty agreeing, that we ask them if they have reached a partial verdict as to either defendant or as to either specification of fraud as to either defendant.

THE COURT: I am not so sure but what they have answered that already. I don't think we can assume they have agreed on part of the case. That isn't what they say at all.

Mr. Stillman, do you wish to say anything?

MR. STILLMAN: I adopt what Mr. Martin has suggested, your Honor. I do object to what Mr. Velie has suggested.

THE COURT: I could sort of anticipate that. I am more interested in any views you may have on your own.

MR. STILLMAN: I think Mr. Martin has expressed my views, your Honor. I think, as your Honor characterized it, a modified Allen charge at this stage of the game would

be in order. I think the idea of luncheon for these people is also probably a good idea just to give them a chance to take a deep breath and without coming at each other.

THE COURT: All right.

MR. VELIE: Your Honor, perhaps the thing to do to simply ask the foreman if they have a preference about lunch. Maybe they can help us.

THE COURT: All right. We will have the jury come in.

xx (Court's Exhibit 7 marked for identification.)

MR. MARTIN: I don't know what your Honor's modified charge is. I certainly hope that it would be simply limited to the fact that you would like them to continue their deliberations without a great deal more from the Allen case.

THE COURT: All right.

(Jury present.)

THE COURT: Mr. Lights and ladies and gentlemen, we have your note. I propose to ask you to continue to deliberate. I point out to you, which I am sure you understand and recollect, but it may be worth noting, that you really haven't been deliberating very long.

Second of all, I point out to you that there doesn't seem to be any indication so far as I can see, that

the parties have not brought before you just about as much evidence as could be brought before you or that they have overlooked any arguments or that if we were to have the case reviewed for us here that anything more could be brought to bear of any particular substance one way or another that has not already been brought to bear.

Of course, as you know, the parties would like a resolution, if possible, of their controversy.

You understand all that. I point out to you that while the verdict of you the jury should represent the opinion of eachindividual juror, it by no means follows that opinions may not be changed by conference, robust discussion, indeed, even argument in the jury room. The very object of the jury system is to secure unanimity by a comparison of views and by discussion and argument among the jurors.

It certainly cannot be the law that each juror should not listen with deference to arguments and with a distrust of his own views, his own judgments, if he finds that a substantial number of the juror members with him take a different view of the case from that which he or she takes.

It cannot be that each juror should go into the jury room with a blind determination that the verdict shall represent his or her opinion of the case at the moment or

that he or she should close his or her ears to the arguments of others who are equally concerned, honest and intelligent as himself.

Keep in mind that at all times no juror is expected to yield a conscious conviction he or she may have as to the weight or effect of the evidence, but remember also that after full deliberation and consideration of all of the evidence it is your duty to agree upon the verdict if you can do so without violating your individual judgment and conscience.

Now, I think it might be very helpful if we had the marshal escort you to luncheon now, give you a chance to get a breath of fresh air on a nice day, have a nice lunch, I hope, and then I am going to ask you to come back and resume your deliberations.

We all know how conscious, thoughtful and attentive you have been, and we understand your note, but I am going to ask you to continue to deliberate. I have confidence that you will keep in mind these instructions I just gave you and think about it, discuss it. Try to view the evidence as a whole, try to view my instructions of law as a whole. I am confident that you will be able to agree on a verdict as to one or both of the defendants.

Very good. Yes, Mr. Lights.

JUROR NO. 1: Would you be kind enough and would it be in order to ask you to once again explain the term "knowing."

THE COURT: It certainly is very much in order and I would be more than happy to do that.

In the context of this case, ladies and gentlemen, a defendant may be found to have acted wilfully and knowingly only if he knew that a portion of the financial statement, such as a footnote or some other entry, was false and misleading. It is not enough merely to establish that a given defendant acted negligently or through error or mistake.

A finding of an intention to include false or misleading information of a material nature is required. Good faith, that is to say, an honest belief in the truth of the data set forth in the relevant footnote and entries in the proxy statement, would constitute a complete defense here.

In this connection, I point out to you that the prosecution is not required to prove the making of the alleged false or misleading statements or the defendants knowing and intentional participation therein by direct proof, that is to say, by direct evewitness evidence or the like.

Such elements obviously may be proved by circumstantial evidence, by such inferences, in other words, as may naturally and reasonably be drawn from all of the facts and circumstances introduced into evidence.

While I have stated that negligence or mistake do not constitute guilty knowledge or intent, nonetheless, you are entitled to consider in determining whether a defendant acted with intent or knowingly if he deliberately closed his eyes to the obvious or to facts that certainly would be observed or ascertained in the course of his accounting work or whether he recklessly stated as facts matters of which he knew full well he was ignorant.

If you find such reckless deliberate indifference to or disregard for truth or falsity on the part of a defendant, the law entitles you to infer therefrom that the defendant wilfully and knowingly filed or caused to be filed false financial information with the SEC. But such an inference, of course, must depend upon the weight and credibility extended to the evidence of recklessness and indifference.

As stated, ordinary or simple negligence alone would be insufficient to support a finding of guilty knowledge or wilfulness.

Now, you remember I said a good deal more. I

went on to discuss, for example, in this general area the question of whether or not a given defendant conformed with or followed generally accepted accounting principles and what weight that might bear in making this determination of wilful and knowing conduct.

If you would like, I will repeat all that.

Have I convered, Mr. Lights, what seemed to be on your mind, sir?

JUROR NO. 1: Yes.

THE COURT: Is that all right?

JUROR NO. 1: Yes, sir.

THE COURT: All right. If there is anything else that occurs toyou in my charge that you would like me to repeat, why, don't hesitate to let me know. But I think now is a good time, unless you have something else on your mind, for you to go outto luncheon. Keep my remarks of a moment ago about the obligation and concerns of jurors in your deliberations in mind when you return from lunch.

Very good.

Marshal, would you escort the jury to lunch.

(The jury left the courtroom.)

THE COURT: Any exceptions?

MR. MARTIN: Yes, your Honor. I want to except to your Honor's inclusion of the reckless disregard language

in the charge, as I did at the time it was given, your Honor.

THE COURT: Yes. Exception to your client.

Anything else, gentlemen?

MR. STILLMAN: I join in that, your Honor.

THE COURT: All right, sir. I think that should be made clear of record. Good for you. Exception to your client.

Now, I would judge that if you could all be back a few minutes before 2 that would seemingly be about right.

MR. MARTIN: Thank you, your Honor.

MR. VELIE: Thank you, your Honor.

(Luncheon recess.)

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AFTERNOON SESSION

(In open court. Jury roll called -- all present.)

THE CLERK: Mr. Foreman, has the jury reached a verdict as to each defendant?

THE FOREMAN: Yes.

THE CLERK: How do you find as to Defendant Natelli?

THE FOREMAN: We find Natelli guilty.

THE CLERK: How do you find as to Defendant Scansaroli?

THE FOREMAN: Guilty.

THE CLERK: Members of the jury, please listen to your verdict as it now stands recorded. You say you find the defendants Natelli and Scansaroli guilty and so say you all?

MR. MARTIN: May we have the jury polled, your Honor?

THE COURT: Yes.

THE CLERK: Members of the jury, listen to your verdict as it now stands recorded.

You say that you find the defendants Natelli and Scansaroli guilty.

(Each juror, upon being asked "Is that your verdict," answered in the affirmative.)

THE COURT: Mr. Lights, and ladies and gentlemen, I want to wish you well and to thank you for your service. We weren't able to complete quite as quickly as we hoped and told you we planned when we started.

I realize that this has been not entirely easy for any one of you. Somehow I have had the sense in getting to know you through some sort of osmosis in recent weeks that you are a most agreeable and punctual and attentive jury. I mean this. It isn't just for the record. I just had a sense of pleasure in working with you. I would hope that I could work with you again. Perhaps that is something that you just as soon avoid, but I really mean it from my viewpoint.

This has been high public service. It is a matter of great importance that jurys participate in our system. Quite frankly, though I am a professional judge, I would not like to see the system be a system in which nobody but lawyers and professional judges had the say in these cases.

I salute you and wish you godspeed in your separate endeavors as I say goodbye.

(Jury excused.)

THE COURT: Gentlemen, I am fixing December 27 at 2:15 o'clock in room 1105 in this building for sentence.

I take it that the bail arrangements, whatever they may be, can be continued without opposition from the prosecution.

MR. VELIE: Yes, your Honor.

THE COURT: All right. Is there something you want, Mr. Martin?

MR. MARTIN: I just want to have until that time also to make any motions that we are entitled to make. Is that agreeable, your Honor? Or to a week before that time

THE COURT: Did you hear that, Mr. Stillman?

MR. STILLMAN: I did, your Honor. I would like to have those motions returnable at some time before that s... that it doesn't set up a crowded day.

THE COURT: There is ample time. I put the matter over quite a long time because of the holidy season. I expect to be here, but as you know, there did seem to be some sense to putting this beyond Christmas, for obvious human reasons. I would be willing to have the motions orally or in writing, as you choose. Would you like to have them on the previous Friday, which would be the 20th?

MR. MARTIN: Your Honor, can you extend the time and give us a little time -- we have the other one motion that is still pending.

THE COURT: I am going to rule on that right now.

I am interested now in other motions. I suggest the 20th, in which case I would ask you to serve and file your papers ten days in advance thereof.

MR. MARTIN: Fine, your Honor. That is agreeable.

THE COURT: Do you want to do it orally? You certainly can.

MR. MARTIN: That is agreeable, your Honor. We will serve on the 10th and have it on the 20th.

THE COURT: I repeat, in addition to the time sequence, if you would like to do this orally, I would have no objection, so long as you notify Mr. Velie ten days in advance so he can answer you orally.

MR. MARTIN: Fine, your Honor.

THE COURT: Either way.

MR. STILLMAN: I seem to have my calendar fouled up here. What is the date that you have fixed for sentence.

MR. MARTIN: The 27th.

THE COURT: Motions on the 20th.

MR. STILLMAN: Motions on the 20th.

THE COURT: 2:15 o'clock, again, the same room, 1105. Serve your papers on Mr. Velie's office no later than the 10th, or if you want to do this orally notify him in substance what you are raising so that he can be respon-

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sive on the 20th.

Now, there is pending a motion of the defense to dismiss because of the publicity which pertained in an article in the Wall Street Journal. I need not delineate it any more here. You know what I am talking about. I deny that motion.

First of all, I know of no case authority squarely in point, although I am aware of the obiter dicta in the cases which the defense brought to my attention. But I do not believe that those dicta are sufficient unto the event here, most particularly because I do not think there is a shred of evidence that that article came to the attention directly or indirectly of the jury which tried this case and I base that, of course, upon the voir dire of the jury which was conducted some days after the appearance of that article.

I decline also to hold an evidentiary hearing on the matter, for a number of reasons, most particularly because of what I just stated, that either version one takes, that of Burton or that of the reporter who write the article, I do not think that that event or that article infected the jury at all in our case.

Therefore, it seems to me to hold an evidentiary hearing in a busy court like this would be an improvident

waste of court time and manpower. The defendants, of course, collectively, have an exception to that ruling.

Now, even though I have made that ruling I am still going to think about what other steps, if any, perhaps ought to be taken by the Court. I am frank to say I don't know really that there are any steps, but I think that is a problem of the Court, and if anything further is done I will notify counsel as a matter of courtesy, at least, so that you can be heard if you care to be.

Now, the defendants will be continued in the bail arrangements which are already fixed. I am frank to say I do not recall what they are.

MR. MARTIN: There is a personal recognizance bond that each of them has already signed, your Honor.

I don't know what your Honor's intention is with regard to a pre-sentence report. We would be prepared --

THE COURT: My practice is to reveal the pre-sentence report to all counsel and the parties involved and I will have them available in my chambers as soon as they are reported, at which time I welcome you to come and peruse them. When I say "you" I don't mean just you gentlemen who are counsel, I mean the defendant in question.

MR. MARTIN: Fine, your Honor.

THE COURT: Not only that. If any party wishes

to submit any letter ormemorandum on the sentencing issue I would certainly not be anything but receptive to that type of submission.

I would suggest for the moment you might like to wait and see a bit what developes before you decide what to do, and then when you do decide, why, just simply let me know and I am sure we can work it out.

Any other business we need take up today in thi. case?

MR. MARTIN: No, your Honor.

THE COURT: Gentlemen, another day.

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MORRISON, PAUL, STELZMAN & BEILEY

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA	Before: HON. HAROLD R. TYLER JR. District Judge and a Jury
vs.	
ANTHONY M. NATELLI, et al.,	
Defendants.	74 CRIM. 43

New York, November 5,6,7,8, 1974

STENOGRAPHER'S MINUTES

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UNITED STATES OF AMERICA

vs. 74 Cr. 43

ANTHONY M. NATELLI, et al.

MR. MARTIN: Your Honor, the motion I wanted to take up in the absence of the jury in the robing room has to deal with the articles in the Wall Street Journal.

I would request that matter not be typed in the transcript so we don't get into a story on my motion and that is the reason I asked to bring it up. I would like to have to tomorrow to present a brief on the point. I think our basic point, your Honor, is that given the fact that Mr. Burton is chief accountant of the SEC making this statement at a time when the trial was about to commence, it's the second time he has made such a statement during the pendency of this indictment as far as we have been able to determine, that we would move to dismiss the indictment on that ground.

And I would put all that in a motion tomorrow, if I may, and I just want to bring it to your attention so I would not be deemed to have sat on my rights.

THE COURT: Whenever you want to make a motion and you are ready, you tell me. What I would really like to know, is, I don't know of any statements by Burton except

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one.

MR. MARTIN: That will be contained in the papers I will file. We are aware of another incident.

THE COURT: Is there any article that appeared in this morning's Journal?

MR. MARTIN: I did not get any paper this morning, your Honor. The station was out of it.

MR. STILLMAN: I got it, I read it, there was none.

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UNITED STATES OF AMERICA

vs. 74 Cr. 43

ANTHONY M. NATELLI, et al.

(In the robing room.)

MR. RAKOFF: Your Honor, we were served before lunch, as your Honor was, with this memorandum of the defendants to dismiss the indictment on the grounds of the statement made to the press by Mr. Burton.

On the very second page of that there is a paragraph that says, "In addition, other information has come to our attention which indicates that this is the second time that Mr. Burton has publicly expressed his opinion on the merits of this, since this indictment was filed."

And there are other statements of that kind in the statement of facts.

Your Honor, there is no affidavit, and, what's more, there is nothing here giving what was said, who it was said to, when, where or any of the details. I don't see how the Government can possibly respond.

THE COURT: This is the same thing I asked the other day. We still haven't gotten an answer.

MR. MARTIN: May I be heard on that, your Honor?

THE COURT: Quickly.

MR. MARTIN: Basically I took the position in the memorandum that on what we have already we were entitled to a dismissal. I did urge -- if your Honor didn't agree with that, there would be a hearing because there was other information. I will be happy to state it for the record.

I have been advised, your Honor, that Mr. Burton did make a statement and a speech in I believe it was Memphis, Tennessee in February of this year, about this matter and stated that he wouldn't have referred to these cases if these people weren't guilty.

THE COURT: Would you bring the jury in, please.

MR. MARTIN: Also I have been advised by Mr. Earle, counsel for Peat, Marwick, that Mr. Burton made a similar statement in connection with a pending civil case and that at that time Mr. Earle advised Mr. Burton that it was improper to comment publicly upon matters which were before the Court.

Those are the bases for the statements that are contained in the affidavit which we would be prepared to take up at a hearing if your Honor would order it. I ask this not be transcribed.

THE COURT: Yes, it will not be transcribed and you will not reveal any of this memoranda to anybody, and I mean to anybody outside of the people in this room.

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UNITED STATES OF AMERICA

vs. 74 Cr. 43

ANTHONY M. NATELLI, et al.

(In the robing room.)

THE COURT: First of all, Mr. Andrews, gentlemen, of the Wall Street Journal has filed an application with me. He is almost as regular as counsel are in these early morning applications. His application is to see the memorandum that Mr. John Martin filed yesterday.

MR. MARTIN: I would say that the application is denied without prejudice to his right to renew at some future time after the conclusion of these proceedings.

THE COURT: I am not sure I understand you. You ran that by a little too fast. Say that again.

MR. MARTIN: I say I would suggest that he be advised that that application is denied at this time without prejudice to the right to renew it at some time after the termination of these proceedings.

THE COURT: That's fair enough. The real point is that he wants to see the brief.

MR. MARTIN: My reaction to that would be not, your Honor. I think we are taking these matters in here to avoid any additional publicity in this regard.

THE COURT: All right. I think that's probably sensible.

Do you disagree with that, Mr. Velie?

MR. VELIE: No, not really.

THE COURT: All right. Then I will handle it accordingly.

The next thing is, Messrs. Martin and Stillman and Velie, do you want me to bring the jurors in and individually question them as to whether or not they have read anything or seen anything, any publicity on this case?

MR. MARTIN: I think I can speak for Mr. Stillman and our clients, your Honor, to say that we discussed this and we would suggest the following procedure. That the Court in the absence of counsel, speak to eachjuror individually to ask them if they have read or heard anything about the case and if they have, to determine what it is that they have read or heard, and also, if they have read or heard anything, whether in their view this would in any way prejudice their assessment of this case.

THE COURT: I will be glad to do it. I prefer that you listen to this.

MR. MARTIN: I thought, your Honor, it might be less imposing for the jurors involved to have it just with the Court. Obviously your Honor could then report to us

anything that has come up as a result of that.

MR. VELIE: I think that's acceptable procedure if the Court wishes to follow it.

THE COURT: I think it would be helpful, because I am frank to say that I don't have any convictions at all that this jury has gone out and ignored the directions of this Court. My experience is that jurors don't normally do that.

Second of all, I am not at all convinced that the so-called offending article is really unfavorable to the defense. As a matter of fact, if I were in Mr. Velie's shoes, I would be more concerned because of the what I consider to be rather slanted version of other things that went on in the courtroom in favor of the defendants, according to the writer.

So to me this whole thing is a bit of a peculiar problem, and I put the word "problem" in quotes. I am not even sure it is a problem.

But I will be glad to do this because I think it is the first thing that has to be done. Then we can decide on the basis of what happens and on other grounds, whether we have to have a hearing later, as you suggested last evening. That may still be in order. I just don't know at this moment.

MR. MARTIN: Fine, your Honor.

Your Honor, just as a matter of timing, I think any time today that your Honor thinks convenient.

THE COURT: I think what I will do is proceed to do it right now.

MR. MARTIN: Shall we then depart, you Honor?

THE COURT: Yes.

(Counsel left the robing room.)

(Juror No. 1 present.)

xx BY THE COURT:

Q Hello, Mr. Lights. I am sorry to disturb you, but I am calling each member of the jury in to simply ask at this point whether or not you have seen any newspaper article about this case since we started?

A No, I haven't.

Q Or had occasion to see anything on television, even fleetingly, or heard anything on the radio?

A No. There is a young lady on my job who wanted to tell me what she read in the Wall Street Journal, but I told her not to tell me.

Q I am pretty sure everybody is in the same position?

A I don't read the Wall Street Journal.

Q I understand. Nor do I, as a normal matter.

I am pretty sure this is so, but for various legal reasons I am making the inquiry very briefly before we begin today.

Thanks so much. We are going to get everybody to come in in order and then we will start.

(Juror No. 1 left the robing room.)

(Juror No. 2 present.)

BY THE COURT:

Q Good morning, Mr. Napoli.

Mr. Napoli, very simply, I am calling each member of the jury in to find out if by chance since we began the case you have seen anything or read anything in the newspapers or heard anything on television or radio about this case.

A No, sir, I haven't.

Q Very good. I don't have any reason to believe anybody has, but I just want to make sure for various technical reasons.

Thank you, sir. What we are going to do is go through this procedure and then we will start very shortly.

(Juror No. 2 left the robing room.)

(Juror No. 3 present.)

BY THE COURT:

Q Good morning, Mrs. Sanford.

Mrs. Sanford, what I am asking very simply is

whether or not anybody has seen or read anything in the newspapers or heard anything on the radio or television about this case since we began.

A No, but I understand from my father that it has been in the paper.

Q Yes. But you yourself have not --

A No, I haven't read it.

Q I rather thought so, but I want to go through and check with everybody before we begin this morning.

A All right.

Q Thank you so much.

(Juror No. 3 left the robing room.)

(Juror No. 4 present.)

BY THE COURT:

Q Good morning.

A Good morning, Judge Tyler.

Q Mr. Hajek, I just want to ask each member of the jury before we begin today, whether or not since the case began any of you have seen or read anything in the newspapers about the case or heard anything on TV.

A No, I didn't see anything. I was anxious to look, but I couldn't see nothing.

Q All right. Thank you very much.

(Juror No. 4 left the robing room.)

(Juror No. 5 present.)

BY THE COURT:

Q Good morning, Miss Rosenwald. I am asking each member of the jury before we begin today, whether or not since the case began any of you have read anything or seen anything in the newspapers or heard anything said over the radio or television about the case?

A I haven't heard anything and I have avoided looking in any areas where I might find anything. So I don't know whether there is any overt publicity or not.

Q I understand. I rather think that is pretty much what everybody has had in mind, but I just wanted to go through it for technical reasons.

Thank you. We will begin as soon as we finish.

(Juror No. 5 left the robing room.)

(Juror No. 6 present.)

BY THE COURT:

Q Good morning. How are you this morning?

A Fine.

Q I am calling each member of the jury in simply to ask whether or not since we started the trial anyone of you has seen anything or read anything in the newspapers or has heard anything about this over TV and radio?

A I haven't heard any or read any.

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Q Thank you very much, sir.

(Juror No. 6 left the robing room.)

(Juror No. 7 present.)

BY THE COURT:

Q Good morning, Miss Codrington. I am simply calling each member of the jury in to ask whether or not since the trial began any of you have read anything or seen anything in the newspapers or heard anything about the case on television or radio?

A No, nothing at all.

Q Thank you very much. Sorry to trouble you. We will get started very shortly.

A All right.

(Juror No. 7 left the robing room.)

(Juror No. 8 present.)

BY THE COURT:

Q Good morning, Mrs. Chazin. How are you this nice day?

A Fine, thank you.

Q I am calling each member of the jury in to simply inquire as to whether or not since the trial began any one of you have seen anything or read anything in the newspapers or heard anything about this from other sources, such as television or radio.

A No, I did not.

Q Thank you very much.

A You are welcome.

(Juror No. 8 left the robing room.)

(Juror No. 9 present.)

BY THE COURT:

Q Good morning, Mrs. Dedra. How are you?

A Fine, thank you.

Q I am simply calling each of you in to inquire as to whether or not since we began the trial you have either seen anything or read anything in the newspapers or heard anything about the case, say through radio or television, something of that nature?

A No, I didn't. As a matter of fact, I am very busy. My mother is leaving this morning to Florida, my husband is not feeling that good.

Q You have your hands full?

A Yes, yes.

Q I understand.

A Yes.

Q Thank you very much.

A All right.

Q We will get started very shortly.

(Juror No. 9 left the robing room.)

(Juror No. 10 present.)

BY THE COURT:

Q Hello, Mr. Bustin. How are you today?

A Okay.

Q I am simply calling each member of the jury in to ask whether or not since the trial began any of you have had a chance to be exposed to any newspaper article about the case or perhaps something over radio or television or some other source.

A No, I have not.

Q Very good. Thank you, sir. We will get started shortly.

(Juror No. 10 left the robing room.)

(Juror No. 11 present.)

BY THE COURT:

Q Good morning, Miss Clark.

A Good morning.

Q I just want to trouble you one minute to ask, as I have everybody else, whether or not since the trial began you have had any exposure to any newspaper article about this case --

A No.

Q -- or heard anything on television or radio?

A I don't have television. No.

Q Thank you. We will get started very shortly.

A All right.

(Juror No. 11 left the robing room.)

(Juror No. 12 present.)

BY THE COURT:

Q Hello, Mrs. Cooper.

A Good morning, Judge Tyler.

Q I just want to ask you, as I have been each and every one of you, whether or not since we began you have been exposed to any newspaper article about the case or any other source, such as television or radio, which mentioned the case in any way.

A No, I haven't.

Q Thank you. We will get started soon.

(Juror No. 12 left the robing room.)

(Alternate Juror No. 1 present.)

BY THE COURT:

Q Good morning. How are you?

A All right.

Q I am simply asking each one of you whether or not since the trial began you have had any exposure to any newspaper article about the case or exposure to something like a television mention or radio mention of the case, something of that nature?

A I have not.

Q Very good. We will get started very shortly.

A Thank you.

(Alternate juror No. 1 left the robing room.)

(Alternate juror No. 2 present.)

BY THE COURT:

Q Hello, Miss Spiro. How are you?

A Thank you, yourself?

Q Good. I am sorry to disturb all of you but I am obliged to ask whether or not any of you since the trial began have had any exposure to any newspaper article about the case or, say, any radio or television about the case?

A I definitely have not.

Q Thank you. We will get started very shortly.

(Alternate juror No. 2 left the robing room.)

(Alternate Juror No. 3 present.)

BY THE COURT:

Q Good morning, Mrs. Aronson. I am just calling each one of you to ask whether or not since we began the trial you have had any exposure to any newspaper article about this case or exposure to any other source of information, such as radio or television, about the case.

A Not at all.

Q Thank you very much. We will get started right

away. I am sorry for this delay.

A That's okay.

(Alternate juror No. 3 left the robing room.)

(Counsel present.)

THE COURT: Gentlemen, this process, which has consumed half an hour or more, brings to light the following information.

None of the jurors stated that they had seen or heard anything about this at all from any source of the media. The only two exceptions -- and I put that word in quotes -- are Mr. Lights and Mrs. Sanford, numbers 1 and 3, respectively. Mr. Lights reported that one of his co-workers had said to him that she had read an article or articles in the Wall Street Journal and he says that he told her "Look, I don't want to hear anymore about it. The Judge has asked us not to get into this."

Mrs. Sanford said that her father had reported to her that he had read something about it and she said that she asked him not to go any further, that the Judge had asked the jury not to get into this.

The others all stated unequivocally, as I understood them, that they had not seen or heard anything about it.

Now, I personally, for whatever it is worth, as

one who has gone through this procedure on a number of occasions, did not see or observe or feel anything that led me to disbelieve any of these people. However, I suppose I am not infallible in this or any other matter and I will say no more.

I would suggest that there is no reason to type up or transcribe these notes at this point and unless any counsel disagrees, I will simply direct that this portion of the transcript not be typed up until otherwise ordered by the Court.

MR. MARTIN: Fine, your Honor. I just would add I am not sure that we have made Mr. Burton's signed memoranda a part of the record, which I think should be done.

THE COURT: I had thought I made it a Court's Exhibit.

MR. MARTIN: I wasn't sure of that.

THE COURT: Certainly that was the intention. I quite agree with you.

MR. RAKOFF: It was number 2, as I recall it.

THE COURT: Something of that nature. I would ask -- I know I don't need to -- if all of you could continue to advise me, as John Martin has. I do not read the Wall Street Journal as a matter of course, so I don't see these articles unless you bring them to my attention, as I think

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you understand.

I assume that there have not been any others recently or I would have heard about it.

MR. MARTIN: I think I saw a small one the other day that was so innocuous as to not concern me. I don't think it would concern Mr. Velie.

MR. VELIE: It certainly doesn't concern me.

MR. MARTIN: I would just add for the record, your Honor, that we still press our position on the statement alone and the admitted involvement of Mr. Burton we are entitled to a dismissal.

THE COURT: What I am going to do now is wait and I will take this up with you later, more or less along the lines you suggested last night, and if we have to have a hearing, we have to have a hearing.

MR. MARTIN: Fine. Thank you, your Honor.

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UNITED STATES OF AMERICA

vs. 74 Cr. 43

ANTHONY M. NATELLI, et al

THE COURT: I want to ask you two things.

First of all, I am indebted, I assume, to Mr. Martin for the latest matter in the Wall Street Journal, which I find to be absolutely outrageous, irresponsible, yellow journalism of the worse order, even though I don't think there is anything that anybody can do about it, granting our First Amendment freedoms, and second of all, it wouldn't have any really great impact that I can see because I, whatever you may thing, have utmost confidence in this jury not reading this at all, particularly since the voir dire which was conducted yesterday. But I do express thanks to you. It was you.

MR. MARTIN: Yes, your Honor.

THE COURT: I thank you for that. We will make it, as usual, a Court Exhibit in this case.

I find this absolutely inexplicable, even though so far as I know it is fully protected under the laws and the Constitution of this country. To say that this is anything but outrageous flummery in my opinion, would be wrong.

I don't understand how any responsible paper or reporter could ever do such a thing, unless he is purposely seeking to jimmy the Court or the parties or somebody in this case. It just seems to me unbelievable.

If we have a hearing at the end of this case, believe me, I am going to keep my openings open so far as that reporter and that paper, because there is no source protection problem here. Mr. Burton has revealed exactly who the source was by his own willingness and the investigations of Mr. Rakoff.

We will have to seal this and not transcribe this little session because of the subject, of course.

How Mr. Andrews pieced all this together, I wouldn't know. I should say in fairness to all of you, however, I don't believe any of you blurted this out to him. I think he just pieced it together, because he is certainly an intelligent person, and he probably, knowing that Mr. Martin filed this motion, so called, why he probably pieced it all together by his observations without more here in the courtroom. But we will pass that.

MR. MARTIN: May I just say for the record that I do agree with what your Honor has said and we have no objection to sealing the record and ask for it. Also, I think given the fact that you have conducted a voir dire

of the jury yesterday on this subject, I would not ask to do that again in response to this.

THE COURT: Oh, no. That to me would be wildly impractical, from your viewpoint and everybody else's.

I assume you agree, Mr. Stillman?

MR. STILLMAN: Absolutely.

Due and timely service of ONE copies
of the within APPENDIX - 4 VOLS is hereby
admitted this 2ND day of APRIL 1975

.....
Attorney for APPELLEE